

**GS 003**  
(2015)

**Guidance Statement GS 003**  
*Assurance Relating to Australian Financial  
Services Licences issued under the  
Corporations Act 2001*

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

Draft

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### **AUTHORITY STATEMENT**

The Auditing and Assurance Standards Board (AUASB) formulates Guidance Statement GS 003 *Assurance Requirements for Australian Financial Services Licensees under the Corporations Act 2001* 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>

M H Kelsall  
Chairman - AUASB

## GUIDANCE STATEMENT GS 003

### *Assurance Requirements for Australian Financial Services Licensees under the Corporations Act 2001*

#### **Application**

1. This Guidance Statement (GS) has been formulated by the Auditing and Assurance Standards Board (AUASB) to provide guidance to auditors conducting assurance engagements relating to Australian financial services (AFS) licensees reporting in accordance with the requirements of Chapter 7 of the *Corporations Act 2001* (the Corporations Act) and the associated *Corporations Regulations 2001* (Corporations Regulations).

#### **Issuance Date**

2. This GS is issued on 1 August 2015 by the AUASB and replaces GS 003 *Audit and Review Requirements for Australian Financial Services Licensees under the Corporations Act 2001*, issued in October 2007.

#### **Introduction**

3. In order to provide financial services in Australia, a person or entity is required by the Corporations Act to either hold an Australian Financial Services Licence (AFSL) or be an authorised representative of the AFSL holder. The Australian Securities and Investments Commission (ASIC) has responsibility for assessing and granting AFSLs on the basis of criteria set out in the Corporations Act<sup>1</sup>. In addition, ASIC enforces financial and assurance requirements for AFS Licensees to meet their obligations under the Corporations Act.
4. The assurance requirements relating to AFS licensees may give rise to a number of special assurance considerations. Accordingly, this GS 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 the assurance engagements of AFS licensees.
5. This GS provides guidance for each section of the assurance engagement as required by ASIC form FS 71 *Auditor's Report for AFS Licensee*, except for the reasonable assurance on the financial statements of the AFS licensee, for which mandatory requirements and explanatory guidance are provided in the Australian Auditing Standards (Auditing Standards). The auditor complies with all of the requirements in each of the Auditing Standards relevant to the financial statement audit in determining the audit procedures to be performed in conducting an audit in accordance with Auditing Standards.
6. This GS does not extend the responsibilities of the auditor beyond those which are imposed by Auditing Standards, Standards on Assurance Engagements (SAEs), the requirements of the Corporations Act and the Corporations Regulations, applicable ASIC regulatory documents and class orders.
7. This GS 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;
  - (b) Applicable Standards on Assurance Engagements including ASAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*,

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<sup>1</sup> Part 7.6 Division 4 of the Act.

ASAE 3100 *Compliance Engagements*, ASAE 3150 *Assurance Engagements on Controls*<sup>2</sup>, ASAE 3450 *Assurance Engagements involving Corporate Fundraisings and/or Prospective Financial Information*<sup>3</sup>.

- (c) Applicable ASIC regulatory documents in this area issued from time to time, such as Regulatory Guide 166 *Licensing: Financial requirements* (RG 166) reissued in July 2015 and Pro Forma 209 *Australian financial services licence conditions* (PF 209) reissued in July 2015; and
  - (d) Applicable ASIC Class orders in this area issued from time to time, such as ASIC Class Order CO 13/760 *Financial Requirements for responsible entities and operators of investor directed portfolio services*; CO 13/761 *Financial requirements for custodial or depository service providers*; and CO 12/752 *Financial requirements for retail OTC derivative issuers*.
8. This GS should not be used as a checklist of issues to be considered by the auditor. Furthermore, it is not intended that this GS limits or replaces the auditor's professional judgement and initiative or limits the application of AUASB Standards on such engagements. AUASB Standards contain the basic principles and essential procedures 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 and type of the AFS licensee and the adequacy of its internal control structure.

#### *Legislative Background*

9. The *Financial Services Reform Act 2001* (FSR Act) and the overall AFS licensing regulatory regime which is administered by ASIC, formally commenced on 11 March 2002. The full provisions of the FSR Act are operative for all AFS licensees under Chapter 7 of the Corporations Act.
10. The FSR Act amendments to the Corporations Act introduced a single licensing regime for financial advice and dealings in relation to financial products. The Corporations Act requires a person or an entity that operates a financial services business to hold the AFS licence or be authorised by the AFS licensee.

#### **Definitions**

11. For the purposes of this GS, the following items have the meanings attributed below:
- (a) The term "auditor" is used throughout this GS and is taken to be a registered company auditor.
  - (b) References to Auditing Standards means, where relevant, reference to Australian Auditing Standards and Standards on Assurance Engagements (ASAEs).
  - (c) For the purposes of this GS an assurance engagement means an engagement in which an auditor aims to obtain sufficient appropriate evidence in order to express a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the subject matter information (that is, the outcome of the measurement or evaluation of an underlying subject matter against criteria).
    - (i) Reasonable assurance engagement means an assurance engagement in which the auditor reduces engagement risk to an acceptably low level in the circumstances of the engagement as the basis for the auditor's conclusion. The auditor's conclusion is expressed in a form that conveys the auditor's

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<sup>2</sup> ASAE 3150 is operative for assurance engagements commencing on or after 1 January 2016. Early adoption of ASAE 3150 is permitted only in conjunction with the adoption of revised ASAE 3000 prior to this date.

<sup>3</sup> ASAE 3450 is applicable when providing assurance around the cash needs requirements for AFSLs as required within section 4 of FS 71.

opinion on the outcome of the measurement or evaluation of the underlying subject matter against criteria.

- (ii) Limited assurance engagement means an assurance engagement in which the auditor reduces engagement risk to a level that is acceptable in the circumstances of the engagement but where that risk is greater than for a reasonable assurance engagement as the basis for expressing a conclusion in a form that conveys whether, based on the procedures performed and evidence obtained, a matter(s) has come to the auditors attention to cause the auditor to believe the subject matter information is materially misstated. The nature, timing, and extent of procedures performed in a limited assurance engagement is limited compared with that necessary in a reasonable assurance engagement but is planned to obtain a level of assurance that is, in the auditor's professional judgment, meaningful. To be meaningful, the level of assurance obtained by the auditor is likely to enhance the intended users' confidence about the subject matter information to a degree that is clearly more than inconsequential.

## **Selected Regulatory Requirements for AFS Licensees**

### **Corporations Act Requirements**

- 12. The Corporations Act<sup>4</sup> requires the AFS licensee to prepare and lodge a profit and loss statement and balance sheet with ASIC. In addition, AFS licensees other than limited AFS licensees<sup>5</sup>, are required<sup>6</sup> to lodge an auditor's report in the prescribed form with ASIC for each financial year. ASIC requires the profit and loss statement (Statement of Profit and Loss and Other Comprehensive Income) and balance sheet (Statement of Financial Position) and notes to the Statement of Profit and Loss and Other Comprehensive Income and Statement of Financial Position (the "financial statements") to be attached to the *Australian financial services licensee: profit and loss statement and balance sheet* (FS 70) and accompanying *Auditor's Report for AFS Licensee* (FS 71). Forms FS 70 and FS 71 can be found on the ASIC website [www.asic.gov.au](http://www.asic.gov.au) under "Download Forms".
- 13. Section 989D(1) of the Corporations Act and regulation 7.8.14A of the Corporations Regulations require the AFS licensee to lodge FS 70 and FS 71 with ASIC within the following timeframes:
  - (a) if not a body corporate – the day that is 2 months after the end of that financial year;
  - (b) if a body corporate that is a disclosing entity or a registered scheme – the day that is 3 months after the end of that financial year; or
  - (c) if a body corporate that is not a disclosing entity or registered scheme – the day that is 4 months after the end of that financial year.
- 14. Many AFS licensees lodge annual financial reports and the auditor's report under Chapter 2M of the Corporations Act (within 3 or 4 months of the financial year) with ASIC. The lodgement requirements under Chapter 2M and Part 7.8 of the Corporations Act are independent obligations and so it is necessary for AFS licensees to lodge financial statements separately under both provisions. The lodgement requirements under Chapter 2M of the Corporations Act apply to companies in general and are not affected by the FSR Act amendments. The FSR Act requires AFS licensees to lodge an FS 70 form (which includes the annual financial statements) and an FS 71 form (auditor's report) under Part 7.8 of the Corporations Act. Only the financial reports lodged under Chapter 2M are on public record while FS 70 and FS 71 contain information that is not required under Chapter 2M. If the AFS

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<sup>4</sup> Section 989B(1) and 989B(2) of Part 7.8 of the Corporations Act.

<sup>5</sup> Limited licensees are defined in section 989B(4) of the Corporations Act.

<sup>6</sup> Section 989(B)(3) of Part 7.8 of the Corporations Act.

licensee is not required to lodge annual financial reports under Chapter 2M, they are still required to lodge FS 70 and FS 71 with ASIC under Part 7.8 of the Corporations Act.

15. The AFS licensee can apply to ASIC for an extension of time to lodge FS 70 and FS 71 under Section 989D(3) of the Corporations Act.

### **Financial Requirements for AFS Licensees**

#### *Financial Requirements for APRA Regulated Entities, Market and Clearing Participants*

16. The base level financial requirements (refer paragraph 19) and other financial requirement conditions, as set out in ASIC Pro Forma 209 (PF 209), do not apply but FS 70 and FS 71 are still required to be lodged with ASIC if the AFS licensee is either:
- (a) a body regulated by the Australian Prudential Regulation Authority (APRA) as defined in Section 3(2) of the *Australian Prudential Regulation Authority Act 1998*; or
  - (b) a market participant (other than a principal trader, unless the principal trade is a registered market trader) as defined in section 761A of the *Corporations Act 2001* in relation to a licenced financial market operated by:
    - (i) ASX Limited (ASX market) that is required to comply with, and complies with, the rules of the *ASIC Market Integrity Rules (ASX Market) 2010* that impose financial requirements, taking into account any waiver by ASIC; or
    - (ii) Chi-X Australia Pty Limited (Chi-X market) and APX markets that are required to comply with, and complies with, the rules of the *ASIC Market Integrity Rules (Chi-X Australia Market) 2011* and *APX market 2013* that impose financial requirements, taking into account any waiver by ASIC; or
    - (iii) Australian Securities Exchange Limited (ASX 24 market), that restricts its financial services business to participating in the ASX 24 market and incidental business<sup>7</sup>; and is required to comply with, and complies with, the rules of the *ASIC Market Integrity Rules (ASX 24 Market) 2010* that impose financial requirements, taking into account any waiver by ASIC; or
  - (c) a clearing participant as defined in section 761A of the *Corporations Act 2001* in relation to a clearing and settlement facility (“CS facility”), where that facility is the licensed CS facility operated by:
    - (i) ASX Clear Pty Limited, and the AFS licensee is required to comply with, and complies with, the operating rules of ASX Clear Pty Limited that impose financial requirements, taking into account any waiver of those requirements by ASX Clear Pty Limited; or
    - (ii) ASX Clear (Futures) Pty Limited, and the AFS licensee restricts its financial services business to participating in that CS facility and incidental business; and is required to comply with, and complies with, the operating rules of ASX Clear (Futures) Pty Limited that impose financial requirements, taking into account any waiver of those requirements by ASX Clear (Futures) Pty Limited.
17. Where an AFS licensee is a body regulated by APRA, PF 209 condition 27 requires the audit opinion to state whether for the relevant period, on a reasonable assurance basis, the AFS licensee was a body regulated by APRA throughout the financial year or for any period of time that ASIC requests. ASIC includes this licence condition confirmation as an application

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<sup>7</sup> ASIC Regulatory Guide RG 166.186 explains that the relevant financial requirement in the ASIC market integrity rules may not be sufficient where an ASX 24 participant undertakes additional business.



statement made under section 1 of FS 71. The auditor satisfies themselves that the information included under the application statement is applicable.

18. Where an AFS licensee is a market participant or clearing participant, PF 209 condition 27 requires the audit opinion to state whether, during any part of the period for which the AFS licensee relied on being a market participant or clearing participant, on a reasonable assurance basis, the AFS licensee was a participant in the market conducted by:
- (a) ASX; or
  - (b) Chi-X market; or
  - (c) ASX 24 market, and restricted its financial services business to participating in the ASX 24 market and incidental business; or
  - (d) Licensed CS facility operated by ASX Clear Pty Limited; or
  - (e) Licenced CS facility operated by ASX Clear (Futures) Pty Limited, and restricted its financial services business to participating in the licensed CS facility and incidental business; or
  - (f) APX market.

ASIC includes this licence condition confirmation as an application statement made under section 1 of FS 71. The auditor satisfies themselves that the information included under the application statement is applicable.

19. All AFS licensees that are not exempt from the base level financial requirements are required to comply with these requirements under the Corporations Act. The base level financial requirements (summarised in Appendix 3) include:
- (a) the solvency and positive net assets requirements;
  - (b) the cash needs requirement (appendix 6), unless a tailored cash needs requirement applies (refer paragraph 21 and 22).
20. In addition, there are financial requirements specified in PF 209 and RG 166 for:
- (a) trustee companies providing traditional services (net tangible assets requirement, refer to PF 209 condition 19B and RG 166 Appendix 5);
  - (b) issuers of margin lending facilities (net tangible assets requirement, refer to PF 209 condition 19A and RG 166 Appendix 6);
  - (c) foreign exchange dealers (tier one capital requirement, refer to PF 209 condition 20 and RG 166 Appendix 7);
  - (d) holding client money or property (tiered surplus liquid funds requirement, refer to PF 209, condition 21 and RG 166 Section C);
  - (e) transacting with clients as principal (adjusted surplus liquid funds (ASLF) requirement, refer to PF 209, condition 22 and RG 166 Section D); and
  - (f) reporting triggers for AFS licensees who are not APRA regulated and are not retail over the counter (OTC) derivative issuers (refer to PF 209, conditions 23-26 and RG 166.83).

*Financial Requirements for Responsible Entities, Operators of Investor Directed Portfolio Services (IDPS), Custodial or Depository Service Providers and retail OTC Derivative Issuers*

21. In addition to the standard solvency and positive net assets requirements specified in paragraph 19, tailored financial and assurance requirements mentioned in paragraph 22 apply to the following types of AFS licensees:
- (a) A responsible entity authorised to operate a managed investment scheme and IDPS operators.
  - (b) Custodial or depository service providers.
  - (c) Retail OTC derivative issuers.
22. Tailored financial and assurance requirements that apply to AFS licensees mentioned in paragraph 21 include:
- (a) tailored cash needs requirement;
  - (b) tailored net tangible assets (NTA) requirement;
  - (c) tailored liquidity requirement; and
  - (d) tailored assurance requirement.

Refer Appendix 3 for more details and relevant regulatory references.

#### **FS 71 Auditor Reporting Requirements**

23. The FS 71 auditor's report requires:
- (a) Reasonable assurance on the financial statements (included within section 2 of FS 71).
  - (b) Reasonable assurance on the following matters as stated in Regulation 7.8.13(2) of the Corporations Regulations (included within section 2 of FS 71):
    - (i) the effectiveness of internal controls used by the AFS licensee to comply with:
      - Divisions 2, 3, 4, 4A, 5 and 6 of Part 7.8 of the Corporations Act; and
      - Division 7 of Part 7.8 of the Corporations Act other than section 991A; and
    - (ii) whether each account required by sections 981B and 982B of the Corporations Act to be maintained by the AFS licensee has been operated and controlled in accordance with those sections; and
    - (iii) whether all necessary records, information and explanations were received from the AFS licensee
  - (c) A FS 70 statement relating to dealing with clients' money and other property of clients (section 3 of FS 71).
  - (d) Reasonable assurance that the AFS licensee complies with all the financial requirements under the licence other than the cash needs requirement, except for paragraph (e) of the definition of Option 1<sup>8</sup> if the AFS licensee purports to comply with Option 1. A combination of Reasonable and Limited Assurance in relation to the relevant cash needs requirements (options 1-5<sup>9</sup>) as outlined in Appendix 6 is required if the AFS licensee, is not a body regulated by APRA or a market or clearing

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<sup>8</sup> As defined in ASIC PF 209 terms and definitions.

<sup>9</sup> As defined in ASIC PF 209 terms and definitions.

participant or a body subject to tailored cash and audit requirements (refer paragraph 19(b)) (included within sections 4 and 5 of FS 71).

- (e) Reasonable assurance that the AFS licensee complies with all the financial requirements under the licence other than the cash needs requirement, except for paragraph (e) of the definition of Option 1<sup>10</sup> if the AFS licensee purports to comply with Option 1. A combination of Reasonable and Limited Assurance in relation to the relevant tailored cash and audit requirements as outlined in Appendix 4 and 5 is required if the AFS licensee is a responsible entity, an operator of IDPS, a custodial, a depository service provider or a retail OTC derivative issuer, that is subject to tailored cash and audit requirements (included within sections 4 and sections 6-8 of FS 71).
  - (f) A report that there are no matters that should have been reported to ASIC in accordance with section 990K of the Corporations Act during or since the financial year that have not previously been reported to ASIC, other than the matters detailed in FS 71 (section 11 of FS 71).
24. ASIC *Pro Forma 209 Australian Financial Services Licence Conditions* (PF 209), reissued in July 2015, sets out the standard licence conditions which subject to individual circumstances, will usually be applied to licences authorising a person to provide financial services under the AFS licence. It is important that the individual AFS licence conditions are examined carefully so that the appropriate reporting and auditing obligations are met.
25. In addition, ASIC Class Orders CO 12/752, CO 13/760, CO 13/761 set out the financial requirements applicable to specific categories of AFS licensees. It is important that these tailored requirements are examined carefully so that the appropriate financial and auditing obligations are met.

#### *Exemptions From Lodging Form FS 71*

26. The holder of a limited AFSL is not required to lodge FS 71 with ASIC. Regulation 7.8.12A and 7.8.13A of the Corporations Regulations exempts limited AFS licensees<sup>11</sup> from lodging an auditor's report with ASIC but requires the lodgement of a compliance certificate with ASIC. Under section 989B(1) and 989B(2) of the Corporations Act, limited AFS licensees are still required to prepare and lodge with ASIC, a profit and loss statement and balance sheet in the approved form FS 70 within the required timeframes.
27. A foreign Authorised Deposit-taking Institution ("ADI") which holds the AFS licence that has relief under Class Order 03/823 *Relief from licensing, accounting and audit requirements for foreign authorised deposit-taking institutions*, is not required to lodge FS 71 with ASIC. It is exempt from the requirements of section 989B of the Corporations Act, where equivalent reports prepared for the overseas regulator of the foreign ADI are lodged with ASIC at least once in every calendar year and at intervals of not more than 15 months.
28. Where the foreign ADI is also regulated by APRA and the AFS licence contains condition 27 in PF 209, then it is necessary for the foreign ADI to lodge an audit report (even if the foreign ADI is exempt under Class Order 03/823), that states whether for the relevant period, on a reasonable assurance basis, the AFS licensee was a body regulated by APRA at the end of the financial year or for any period of time that ASIC requests. This is because the APRA regulation confirmation requirement is in addition to Section 989B of the Corporations Act or Class Order 03/823. The format of this audit report does not need to be in accordance with FS 71. To avoid any processing problems, ASIC requires the audit report to be lodged and accompanied by a letter identifying the AFS licensee, licence number and financial year, and clearly stating the reasons why FS 71 has not been lodged. ASIC requires this letter to include reference to the class order and to the requirement for a report pursuant to the relevant licence condition.

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<sup>10</sup> As defined in ASIC PF 209 terms and definitions.

<sup>11</sup> Limited licensees are defined in section 989B(4) of the *Corporations Act 2001*.

29. Class Order 06/68 *Conditional relief for foreign licensees from financial reporting and record keeping obligations*, issued 3 February 2006 provides that a foreign company AFS Licence holder (other than a foreign ADI) can lodge accounts prepared for their home regulator with ASIC to meet their AFS Licence requirements. As a result the foreign company does not have to comply with regulations made for the purposes of sections 989B and 989C of the Corporations Act and hence is not required to lodge FS 70 or FS 71.
30. RG 166.19 also states that if the licensee is prudentially regulated overseas, they can apply to ASIC for relief from the financial requirements. ASIC will give this relief on a case-by-case basis if they are satisfied that the applicant is regulated in a way that is comparable to regulation by APRA for entities of that kind. If applicable, ASIC will consider the extent to which the relevant foreign prudential regulation is consistent with the Basel Committee guidelines for regulating deposit-taking institutions.

## **Considerations for the Auditor**

### **Those Who May Audit the AFS Licensee**

31. Section 990B(1) of the Corporations Act, requires the AFS licensee to ensure that at all times a registered company auditor who is not made ineligible through regulation 7.8.16(1)(a) of the Corporations Regulations is engaged to audit the AFS licensee's financial statements.

### **Agreeing on the Terms of the Engagement**

32. The auditor complies with the requirements and guidance contained in ASAE 3000 when agreeing on the terms of the AFS licensee's assurance engagement in writing. Such terms may be outlined in an engagement letter<sup>12</sup>, an example of which is provided in Appendix 1 to this GS. ASA 210 *Agreeing the Terms of Audit Engagements* contains information that the auditor may find helpful when agreeing on the terms of the engagement in this context.
33. The auditor may also use the engagement letter to clarify the respective roles of the AFS licensee and the auditor. In particular, it is important to highlight in the engagement letter the AFS licensee's obligation to establish and maintain effective internal control in relation to compliance with the requirements of the Corporations Act. It is the responsibility of the AFS licensee to comply with all the conditions under its AFSL, including all the financial requirements. As part of the acceptance of the assurance engagement, the auditor may consider obtaining acknowledgment of this obligation from those charged with governance of the AFS licensee when obtaining agreement on the terms of the engagement.

### **Planning**

34. The auditor plans the engagement in accordance with ASAE 3000 and ASAE 3100. In planning 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, that guides the development of the engagement.
35. ASA 315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment* contains information that the auditor may find helpful when obtaining an understanding of the entity and its environment, including its internal controls, to provide a basis for the identification and assessment of the risks of material misstatement of ASIC form FS 70, compliance with the conditions of the Licensee's AFSL and the requirements of Part 7.8 of the Act whether due to fraud or error, and sufficient to design and perform further audit procedures which may also impact on the FS 71 audit report.

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<sup>12</sup> Or other suitable form of audit contract.

*Understanding the Entity and its Environment*

36. In gaining an understanding of the entity and its environment, the auditor can draw on knowledge gained as part of the annual financial statement audit, however this understanding needs to be updated and broadened to meet the requirements of an engagement of AFS Licences issued under the Corporations Act. ASAE 3100<sup>13</sup> provides a list of matters to be considered by the auditor in understanding the entity and the compliance framework. It is likely the auditor will conduct the following procedures in obtaining that increased understanding and assessing risk: enquiries, analytical procedures, observation and inspection.
37. For a limited assurance engagement the auditor does not normally develop the depth of understanding of internal controls in relation to those areas subject only to limited assurance, as is required in a reasonable assurance engagement and so gaining an understanding may be limited to enquiries.

*Identifying and Assessing Risks of Compliance Breach*

38. The auditor of the AFS licensee may consider:
- (a) Key responsibilities and risks identified;
  - (b) Processes and reliability of reporting systems established by the AFS licensee to implement the licence conditions; and
  - (c) Processes and adequacy of systems established by the AFS licensee to monitor adherence to the licence conditions and the Corporations Act requirements. The auditor may obtain from management a copy of the licence conditions, together with a written description of the procedures and structures which the AFS licensee has established to ensure compliance with those licence conditions.
39. In planning the assurance engagements and in making risk assessments, the auditor considers various matters including:
- The licence conditions.
  - The nature and extent of any recent changes to the licence conditions and whether any detected breaches are deemed to be reportable in light of the revised licence conditions.
  - The nature of and extent of any changes to, the operations of the AFS licensee itself.
  - Changes to the requirements of relevant AUASB Standards.
  - Changes to the Corporations Act and Corporations Regulations.
  - Changes to relevant ASIC Regulatory Guides and Class Orders.
  - Reports and other documents submitted to the board of the AFS licensee regarding the operation of the licence and its compliance functions.
  - Previous auditor's reports, including the auditor's report on financial statements of the AFS licensee, and related management letters.
  - History of non-compliance with licence conditions.

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<sup>13</sup> See ASAE 3100, paragraphs 28-32 and 50.

*Overall Responses to Assessed Risks of Material Misstatement in FS 70 and AFSL Compliance Breaches and Further Procedures*

40. The auditor designs and performs further assurance procedures which are responsive to the assessed risks of material misstatement or material compliance breach. The auditor chooses a combination of assurance procedures, which may include: inspection, observation, confirmation, recalculation, re-performance, analytical procedures and enquiry.
41. ASAE 3000 clearly differentiates between the objectives of a limited versus a reasonable assurance engagement, and provides detail around the sufficiency of audit 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. 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 for a reasonable assurance engagement. In a limited assurance engagement procedures primarily involve enquiries and substantive analytical procedures and may not include tests of controls.
42. 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 3100 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 there may be a reportable compliance breach. 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 or non-compliant.
43. In a reasonable assurance engagement, procedures may include tests of controls as well tests of detail. 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 tests of details 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 tests of details will need to be increased or modified.

**Materiality**

44. 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, deficiency, deviation or non-compliance of the subject matter in the entity's reports;
  - (b) The scope of assurance work to be performed; and
  - (c) A reasonable basis for evaluating identified misstatements, deficiency, deviation or non-compliance.Materiality is addressed in the context of the AFS auditor's objectives, which are developed having regard to the reasonable expectations of issues that would likely influence the decisions of the user(s).
45. The auditor sets materiality in accordance with ASAE 3000 and ASAE 3100. ASA 320 *Materiality in Planning and Performing an Audit* contains information that the auditor may find helpful in this context. Information may be adapted by the auditor, as appropriate, to the task of judging adherence to the AFS licence and conformity with the relevant provisions in Part 7.8 of the Corporations Act. However, it is not possible to give a definitive view on what may constitute material, other than to suggest that the auditor exercises appropriate professional judgement having regard to the AFS licensee's obligations, together with the size,

complexity and nature of the AFS licensee's activities. The auditor develops separate materiality levels for each section of the engagement.

46. As identified in ASAE 3000 and ASAE 3100, when assessing materiality, the auditor considers qualitative factors as well as quantitative factors. The following are examples of qualitative factors that may be relevant:
- The specific requirements of the terms of the engagement.
  - The magnitude of instances of detected or suspected non-compliance and whether the misstatement affects compliance with a law or regulation.
  - When the subject matter information relates to a conclusion on compliance with law or regulation, the seriousness of the consequences of non-compliance.
  - The nature of a misstatement, for example, the nature of observed deviations from a control when the subject matter information is a statement that the control is effective.
  - The interaction between, and relative importance of, various components of the subject matter information when it is made up of multiple components.
  - Whether a misstatement is the result of an intentional act or is unintentional.
  - The interests of the intended users.
47. 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 or compliance breach remaining undetected to an acceptably 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 or compliance breaches 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.
48. When determining materiality, the auditor considers ASIC Regulatory Guide RG 34 Auditor's obligations: *Reporting to ASIC* that contains information on the obligations of an auditor of an AFS Licensee in terms of breach reporting and ASIC Regulatory Guide RG 78 *Breach reporting by AFS licensees* that contains information on AFS Licensees breach reporting obligations.
49. Although there is a greater risk that misstatements, control deficiencies or instances of non-compliance may not be detected in a limited assurance engagement than an 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.

#### *Materiality and FS 71*

50. An auditor may have concluded that it is appropriate to issue an unmodified opinion/conclusion but during the course of the engagement may have identified misstatements, deficiencies, deviations or compliance breaches that are not material, either individually, or taken as a whole, in the context of the engagement. ASIC requires that these identified non-material misstatements, deficiencies, deviations, compliance breaches or other exceptions/findings are reported to ASIC within section 9 of FS 71.
51. An auditor may have concluded that it is appropriate to issue an unmodified opinion/conclusion but may still have s990K(2) findings that are not considered by the auditor

to be material, that are reportable to ASIC under s990K(2). These reportable breaches that may or may not impact the auditor's opinion/conclusion are reported to ASIC in section 11 of FS 71 (if not already previously reported).

### **Reporting Entity Concept**

52. AFS licensees are required to lodge annual financial statements attached to FS 70 and FS 71. Where AFS licensees have not previously prepared financial statements or, in very rare situations, have previously prepared special purpose financial statements, then the auditor considers whether the AFS licensee is a reporting entity. Guidance as to what constitutes a reporting entity is contained in Statement of Accounting Concepts SAC 1 'Definition of the Reporting Entity' and Miscellaneous Professional Statement APS 1 'Conformity with Accounting Standards and UIG Consensus Views'. The decision as to whether an entity is a reporting entity needs to be made on a case by case basis in accordance with SAC 1 and APS 1. A requirement to prepare and/or lodge a financial report with ASIC pursuant to the Corporations Act does not, of itself, deem that entity to be a reporting entity.
53. In most circumstances the AFS licensee will be a reporting entity and hence lodge "general purpose" financial statements. AFS Licensees general purpose financial statements may be subject to the reporting requirements under AASB 1053 *Application of Tiers of Australian Accounting Standards* and accordingly may be subject to reduced disclosure requirements.

### **Natural Persons**

54. ASIC has issued class order CO 03/748 *Reporting requirements under s989B* on reporting requirements for AFS licensees who are natural persons. A natural person is defined as an individual, as opposed to a company, partnership or trustee. CO 03/748 states that where the licensee is a natural person, the licensee may exclude from the profit and loss statement, the revenue and expense that do not relate to any business of the licensee or all the revenue and expenses that do not relate to a financial services business of the licensee.
55. Alternatively, a natural person licensee can choose not to rely on CO 03/748 and instead include in a profit and loss statement all of their revenues and expenses, whether personal or business. The relief under CO 03/748 is confined to the preparation of the profit and loss statement. ASIC requires a natural person licensee to still prepare a balance sheet that discloses all of their assets and liabilities, including their personal assets and liabilities and the assets and liabilities of any other business.

## **Auditor Reporting Requirements**

### **Reasonable Assurance on Certain Provisions in Part 7.8 of the Corporations Act (FS 71, section 2)**

56. The FS 71 audit report requires reasonable assurance on the control environment to achieve compliance with the requirements of Divisions 2, 3, 4, 5 and 6 of Part 7.8 of the Corporations Act and Division 7 of Part 7.8 other than section 991A. These provisions include:
- Dealing with clients' money.
  - Dealing with other property of clients.
  - Special provisions relating to insurance.
  - Obligations to report.
  - Financial records, statements and audit.



- Other rules about conduct (i.e.: giving priority to client orders, transmission of instructions through licensed markets, maintaining records of instruction, dealing with non-licensees and employees).

*Assurance Considerations*

57. In assessing the control environment, the auditor needs to determine which of the controls at the AFS licensee are necessary to achieve the control objectives relating to compliance with Divisions 2,3,4,4A,5 and 6 of Part 7.8 of the Corporations Act; and Division 7 of Part 7.8 of the Corporations Act (other than section 991A).
58. Where the auditor is unable to identify controls which are suitable or controls as designed are not suitable to achieve a control objective, if operating effectively, this may constitute a deficiency in relation to the suitability of design which would result in the controls being ineffective.
59. The auditor assesses the risk of the controls necessary to achieve the compliance requirements not operating effectively and uses professional judgement in determining the specific nature, timing and extent of procedures to be conducted.
60. Division 2 of Part 7.8 subdivision A and Corporations Regulations 7.8.01 – 7.8.05 relates to handling of client money including:
- What constitutes client money?
  - Establishing an approved trust account.
  - Payment of client money into the trust account within one business day.
  - Circumstances where money can be withdrawn from the trust account.
  - Treatment of interest on client money.
61. The auditor establishes whether the AFS licensee holds client money and determines whether a trust account has been appropriately established for the financial period. The auditor performs procedures to determine whether the AFS licensee has designed controls that are suitable to meet the relevant requirements; and then tests that those controls have operated effectively throughout the period. The auditor may select items for testing described below to obtain evidence regarding the operating effectiveness of the controls:
- to establish whether client money received has been appropriately paid into the trust account.
  - to establish whether withdrawals from the trust account are in accordance with Corporations Regulation 7.8.02. If an AFS licensee does hold client money, the auditor considers whether they also have to comply with the Surplus Liquid Funds requirement.
  - of trust account reconciliations to establish whether client and AFS Licensee money is properly separated, including that non-client money is properly identified and separated on a timely basis in accordance with the Corporations Regulation 7.8.01.
62. Division 2 of Part 7.8 subdivision B and Corporations Regulations 7.8.06 relates to monies paid to an AFS licensee by way of a loan from a client, including:
- What constitutes a loan from a client (excludes deposit and debenture payments)?
  - Establishing an approved trust account.
  - Payment of money lent into the trust account within 1 business day.

- That a statement is required to be given to the client setting out the terms and conditions of use of the loan and the purpose for which funds will be used.
  - The requirement to only use funds for the specified purpose outlined in the terms and conditions or subsequently agreed to in writing.
  - The auditor establishes whether the AFS licensee has received a loan from a client and determines whether a trust account has been appropriately established for the financial period. The auditor performs procedures to determine whether the AFS licensee has designed controls suitable to meet the relevant requirements; and then designs procedures to test that those controls have operated effectively throughout the period. The auditor may perform procedures described below to obtain sufficient appropriate audit evidence regarding the operating effectiveness of the controls:
    - Selecting a sample of items for testing to establish whether money received has been appropriately paid into the trust account;
    - Testing to establish whether clients have been given the appropriate statements;
    - Selecting a sample of items for testing to establish whether money lent has been used for an agreed purpose.
63. Division 3 of Part 7.8 and Corporations Regulation 7.8.07 relates to the handling of property other than money given to the AFS licensee, including:
- What constitutes client property?
  - How the AFS licensee deposits or registers that client property.
  - Circumstances in which an AFS licensee can hold property as security.
  - The requirement to return secured property to the client within one business day of the client settling their obligation to the AFS licensee.
  - The requirement to provide clients with statements of property held as security every 3 months.
64. The auditor establishes whether the AFS licensee handles client property. The auditor performs procedures to determine whether the AFS licensee has designed controls suitable to meet the requirements of Division 3 of Part 7.8 and Corporations Regulations 7.8.07; and then designs procedures to test that those controls have operated effectively throughout the period. The auditor may perform procedures described below to obtain sufficient appropriate audit evidence regarding the operating effectiveness of the controls:
- Selecting a sample of items for testing to establish whether property received has been appropriately deposited or registered;
  - Establishing whether property is received as security;
  - Selecting a sample of items for testing to establish whether the AFS licensee has complied with the requirements relating to property received as security.
65. Division 4 of Part 7.8 and Corporations Regulations 7.8.08 relates to the receipt of monies by AFS licensees who are insurance brokers and agents of general and life insurance contracts but not the actual insurer. Auditors consider the applicable legislation and design appropriate tests to determine whether the AFS licensee has designed controls to meet the relevant requirements and that these controls are operating effectively throughout the period.

66. Division 5 of Part 7.8 makes provision for the regulations to impose reporting requirements in relation to money to which Division 2 or 3 applies, or to an AFS licensee dealing in derivatives. Currently, there are no regulations relating to this Division.
67. Division 6 of Part 7.8 relates to financial records, statements and audit. The auditor considers the applicable legislation and design appropriate tests to determine whether the AFS licensee has designed controls suitable to meet the relevant requirements and then designs procedures to test that these controls are operating effectively throughout the period.
68. Division 7 of Part 7.8 (other than section 991A) relates to other rules about conduct in licensed markets. The auditor considers firstly whether the legislation is applicable to the AFS licensee. If the legislation is applicable, the auditor then designs appropriate tests to determine whether the AFS licensee has designed controls suitable to meet the relevant requirements and then designs procedures to test that these controls are operating effectively throughout the period.

**FS 70 Statement relating to Dealing with Clients' Money and Dealing with Other Property of Clients (FS 71, section 3)**

69. The FS 71 audit report contains a FS 70 statement on paragraphs 7 (whether the AFS licensee received client monies), 8 (whether the AFS licensee received client property) and 9 (whether the AFS licensee received a loan from a client) of FS 70. The auditor considers the AFS licensee's statements on FS 70 and through performing evidence gathering<sup>14</sup> procedures including, knowledge of the client, corroborative enquiry and representations from management, obtains sufficient appropriate audit evidence to conclude whether the statements in FS 70 are appropriate.

**Financial Requirements (FS 71, sections 4-8)**

70. The FS 71 audit report requires a combination of reasonable assurance opinions and limited assurance conclusions on the AFS Licensee's compliance with prescribed financial requirements and other relevant legislation. The auditor considers the relevant financial requirements by referring to the licence conditions and obtains sufficient appropriate audit evidence to reach a reasonable assurance opinion or limited assurance conclusion.
71. Audit evidence may be gathered through enquiry and observation, tests of control, substantive testing and representations from management. The amount of evidence from each source is a matter for the auditors' professional judgement. It is unlikely that sufficient assurance may be obtained from only performing one type of testing. The type and extent of procedures will be based on the complexity of the AFSL, nature of business and initial risk assessment. When auditing compliance with the AFS Licensee's financial requirements throughout the period, it is important for the auditor to:
  - (a) understand how the AFS licensee derives their calculations, so the auditor can conclude as to whether this method is in accordance with the requirements;
  - (b) ascertain whether all the calculations prepared during the period demonstrate a compliant position; and
  - (c) select a sample number of calculations to test for accuracy based on underlying financial information.

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<sup>14</sup> The concepts and discussions on evidence relevant to an audit engagement are contained in Auditing Standard ASA 500 *Audit Evidence*, and contains information and guidance that the auditor may find helpful in determining the evidence applicable to compliance engagements.

*Cash Needs Requirement – Assurance Considerations*

72. ASIC requires reasonable assurance and limited assurance on the entity's compliance with the AFS licensee's financial requirements for the entire year, not just year-end. Hence, evidence-gathering procedures will need to include an understanding of the processes adopted by the AFS licensee to ensure compliance throughout the year, such as formal policies, monthly calculations, use of standard calculation templates and monitoring by the AFS licensee's board or appropriate delegate. The auditor considers testing to be performed on a sample basis depending on the assessment of effectiveness of controls.
73. If the AFS licensee has adopted Option 1 for the cash needs requirement or is subject to a tailored cash needs requirement, the auditor considers compliance throughout the period with the cash holding requirement in Part (e) of the Option 1 definition, or with the cash holding requirement per the applicable ASIC Class Order (CO 12/752 or CO 13/760 or CO 13/761) as appropriate.
74. The auditor considers obtaining the cash flow projections throughout the relevant period and determines whether the cash flow projections are either:
- (a) a projection of the AFS licensee's cash flows over at least the next 3 months based on the AFS licensee's reasonable estimate of what is likely to happen over this term (Option 1); or
  - (b) a projection of the AFS licensee's cash flows over at least the next 3 months based on the AFS licensee's estimate of what would happen if the AFS licensee's ability to meet its liabilities over the projected term (including any liabilities the AFS licensee might incur during the term of the projection) is adversely affected by commercial contingencies taking into account all contingencies that are sufficiently likely for a reasonable AFS licensee to plan how they might manage them (Option 2); or
  - (c) a projection of the AFS licensee's cash flows over at least the next 12 months based on the AFS licensee's reasonable estimate over what is likely to happen over this term; and is approved at least quarterly by those charged with governance (tailored cash needs requirement).

The auditor considers establishing how often and when the cash flow projection is updated to ensure it continuously covers at least the next 3 months (12 months – tailored cash needs requirement).

75. The auditor considers obtaining the AFS licensee's documented assumptions used to prepare the cash flow projections and checking whether the assumptions have been correctly applied in preparing the projections. This may include ensuring that the documented assumptions on the timing of cash flows have been correctly applied to budgeted revenues, expenses and capital expenditure.
76. Based on the cash flow projections already obtained, the auditor considers whether there is evidence that the cash flow assumptions are not appropriately documented or that the projections do not demonstrate that the AFS licensee had access as needed to sufficient financial resources at all times in compliance with paragraphs (b) and (d) of either the Option 1 or Option 2 definitions or paragraphs 3(c) or 3(e)(i) of the tailored cash needs requirements of ASIC Class Orders CO 12/752, 13/760 or 13/761 throughout the period. The auditor considers whether the documentation is sufficient to enable the auditor to ascertain whether the assumptions have been correctly applied in preparing the projections. This may involve reviewing the documentation of budget assumptions if the cash flow documentation does not stand alone. The auditor may consider the use of specialists in this area.
77. Based on reviewing the assumptions in line with the auditor's knowledge of the business and on enquiries of management, the auditor considers whether there is evidence that the assumptions used are unreasonable. This may involve obtaining an understanding of the AFS

- licensee's budgeting process if budgets are used to prepare the cash flow projections, or considering the historical accuracy of the assumptions in predicting actual cash flows.
78. If the licensee relies on Option 2, then based on reviewing the basis of selecting the assumptions in line with the auditor's knowledge of the business and on enquiries of management, the auditor considers determining whether there is evidence that the basis for selecting the assumptions is unreasonable.
79. Under Option 3, where the AFS Licensee does not prepare a cash flow projection, but instead relies on a financial commitment from an Australian ADI, or comparable foreign institution, (under licence condition 13(c)(iii)) the audit report is required to contain a statement about whether the licensee has obtained an enforceable and unqualified commitment to pay on demand from time to time an unlimited amount to the licensee, or the amount for which the licensee is liable to its creditors at the time of demand to the licensee's creditors or a trustee for the licensee's creditors.
80. Where the AFS licensee is a subsidiary of an Australian ADI or ASIC-approved prudentially regulated body that does not prepare cash flow projections, on the basis of its expectation concerning the adequacy of resources (under licence condition 13(c)(iv)), the audit report is required to contain a statement about whether the auditor has any reason to believe that the basis for selecting the assumptions documented by the AFS licensee in forming the expectation is unreasonable.
81. Where the AFS licensee uses group cash flow projections to meet the cash needs requirement, on the basis of alternative A (under licence condition 13(c)(v)), the auditor is required to include an audit opinion on whether the parent entity has provided an enforceable and unqualified commitment to pay on demand an unlimited amount to the AFS licensee, or to meet the AFS licensee's liabilities (including any additional liabilities that the AFS licensee might incur while the commitment applies).
82. In addition, when relying on the Group cash flow projections under licence condition 13(c)(v), the licensee auditor should be mindful of the requirement for the parent entity auditor to provide a separate opinion modelled on the Option 1 or 2 audit requirement and that this audit report is required to be submitted at the same time as the FS 71 opinion (under licence condition 13(c)(v)(D)).
83. Where the AFS licensee relies on alternative B (under licence condition 13(d)(v)), the audit report is required to contain a statement about whether the auditor has any reason to believe that the documented basis for selecting the assumptions, on which the AFS licensee's expectation concerning the adequacy of the resources required under alternative B, is unreasonable.

#### **Limited Assurance on Risk Management Systems (FS 71, sections 4-8)**

84. FS 71 requires limited assurance on risk management systems to ensure ongoing compliance with financial requirements. Section 912A(1)(h) requires the AFS licensee to have adequate risk management systems. To satisfy this obligation, ASIC expects that the risk management systems will specifically deal with the risk that the AFS licensee's financial resources will not be adequate to ensure that they are able to carry on their business in compliance with their licence obligations.

#### *Assurance Considerations*

85. ASAE 3150 requires the auditor to perform procedures to determine whether the AFS licensee has designed controls that are suitable to meet the requirements of section 912A(1)(h) and then designs procedures to test that these controls have operated effectively throughout the period. Having regard to the risk of inadequate financial resources, these procedures may include:
- Obtaining an understanding of the risk management systems (RMS) and the process to identify material risks;

- Consideration as to whether a formal documented risk management system exists, although the formality and extent of the processes required will depend on the size, nature and complexity of the business; and
- Obtaining periodic calculations of compliance with financial requirements, and consideration of processes that may exist to identify and address matters that may arise between these periodic calculations that have the potential to cause non-compliance with the financial requirements, although the extent of these processes will depend on how much of a buffer the AFS licensee has above the requirements and the sensitivity of these buffers to fluctuations in the performance and financial position of the AFS licensee.

There is no expectation that the auditor expresses assurance conclusions on the adequacy of the specific controls of the risk management system.

86. As part of the limited assurance procedures, the auditor may seek the following types of information and documentation:

- Copies of the RMS documents that set out the AFS licensee's RMS during the period;
- Documentation that identifies and describes the systems, policies, procedures and structures that are in place to manage identified risks and representations that such systems, policies, procedures and structures have been complied with;
- Minutes of the meetings of those responsible for monitoring compliance with aspects of the RMS;
- Internal audit reports (if applicable);
- Certifications if made by the AFS licensee and relevant supporting documentation to substantiate compliance with the RMS during the reporting period; and
- Other supporting evidence to confirm that the controls identified in the RMS have been in place during the reporting period.

The above is not meant to represent an exhaustive list and there may be other evidence that is relevant to the specific circumstances of each AFS licensee.

#### **Statement on Section 990K(2) Matters (FS 71, section 11)**

87. FS 71 requires a statement about any matter referred to in section 990K(2) of the Corporations Act and covers the year under audit and up until the date the FS 71 auditor's report is signed. This section 990K(2) statement only deals with those matters that have not already been reported by the auditor as required under section 990K(1). Given the 7 day reporting time frame under section 990K, it is likely that for most matters, the auditor would not wait until they lodge FS 71 to report matters to ASIC. The section 990K(2) statement is not part of the opinion section in FS 71.
88. If a section 990K matter has been reported by the auditor to ASIC, this does not require re-reporting as a specific section 990K matter in section 11 of FS 71. However, such matters may still need to be included in section 2-8 of FS 71 as the basis for a modified opinion/conclusion or in section 9 of FS 71 as a non-material matter.
89. Section 990K(2) requires a report to be given in relation to any matter that, in the opinion of the auditor:
- (a) has adversely affected, is adversely affecting or may adversely affect the ability of the AFS licensee to meet the AFS licensee's obligations as an AFS licensee; or
  - (b) constitutes or may constitute a contravention of:

- (i) a provision of Subdivision A or B of Division 2 (or a provision of regulations made for the purposes of such a provision); or
  - (ii) a provision of Division 3 (or a provision of regulations made for the purposes of such a provision); or
  - (iii) a provision of Subdivision B or C of this Division (or a provision of regulations made for the purposes of such a provision); or
  - (iv) a condition of the AFS licensee's licence; or
- (c) constitutes an attempt to unduly influence, coerce, manipulate or mislead the auditor in the conduct of the audit.

#### *Assurance Considerations*

90. If the auditor becomes aware of the above relevant matters (a) - (c) during the course of the audit of the financial statements, performing work on FS 71 or undertaking other audit work (e.g. Managed investments compliance plan audits), they have an obligation to report on them. If the auditor becomes aware of a section 990K(2) matter that is outside the Corporations Act sections under audit, then the auditor is required to report on these section 990K(2) matters but has no obligation to look for matters outside the sections under audit.
91. Apart from the requirement to report section 990K(2) breaches in FS 71, section 990K(1) requires auditors to report such breaches to ASIC (and the AFS Licensee and any relevant market or clearing authority e.g. ASX for stockbrokers) within 7 days of becoming aware of the matter. Auditors consider this obligation at all times of the year, but particularly during the planning, interim and final stages of their audits. The AFS licensee is required to report any such breaches as soon as practicable and within 10 business days of becoming aware of the matter as required by section 912D(1B). The auditor is expected to report breaches even if the AFS Licensee has already reported same.
92. There is a potential conflict between the auditor's obligation to report *any* breaches and the AFS licensee's obligation to only report *significant* breaches to ASIC. An opinion or conclusion is not provided on the 990K statement in the FS 71. The auditor separately considers whether a matter reported in the statement also impacts the audit opinion within the FS 71 report.
93. As the section 990K(2) statement specifically covers both the financial year and the period between the end of the financial year and the date of signing the FS 71 auditor's report (unlike the other reporting requirements in FS 71), the auditor is obliged to formally consider the existence of relevant matters up to the date of signing the report. To determine the existence of such matters, the auditor considers matters including:
- Reading minutes of the meetings of those charged with governance, and compliance, audit and executive committees, held after the reporting date, and enquiring about matters discussed at meetings for which minutes are not yet available.
  - Obtaining copies of all correspondence with ASIC and any other relevant regulators up to the date of signing.
  - Enquiring of management as to whether any subsequent events have occurred which might represent matters referred to under section 990K(2).

#### **Overall Assurance Reporting Considerations**

94. Due to the nature of audit testing and other inherent limitations of an audit, together with the inherent limitations of the AFS licensee and its related licence conditions, there is a possibility that a properly planned and executed audit will not detect all deficiencies in the AFS

licensee's licence conditions. Accordingly, the audit opinion under section 989B(3) of the Corporations Act is expressed in terms of reasonable or limited assurance (as appropriate) and cannot constitute a guarantee that the AFS licensee is completely free from any deficiency, or that all compliance breaches have been detected.

95. There are also practical limitations in requiring an auditor to perform a continuous examination of the AFS licensee, and form an opinion that the entity has complied at all times with the Corporations Act during the period covered by the AFS licensee audit report. However, the auditor performs tests periodically throughout the financial year to obtain evidence and obtain reasonable assurance that the measures complied with the written descriptions and were adequate throughout the period under examination.
96. Prior to issuing the FS 71 audit report, the auditor considers obtaining a written representation from the directors of the AFS licensee which contains their assertions that the AFS licensee has complied with the licence conditions during the financial year and up to the date the FS 71 audit report is signed, and that the AFS licensee continues to meet the requirements of Part 7.8 of the Corporations Act. In obtaining and using these written representations, the auditor complies with the requirements of, as appropriate, ASAE 3000. An example management representation letter is contained in Appendix 2.
97. The FS 71 audit report is an ASIC prescribed form and can be found on the ASIC web site [www.asic.gov.au](http://www.asic.gov.au) under "Download Forms". ASIC requires form FS 71 to be lodged in the prescribed form and that no modifications or deletions are made, unless consented to by ASIC.
98. It is important to check the ASIC website to ensure that the latest version of FS 71 is adopted.

#### **Communications with Those Charged with Governance**

99. Under ASAE 3000 and ASAE 3100, the auditor communicates relevant matters of governance interest arising from the engagement to those charged with governance on a timely basis. In addition, Auditing Standard ASA 260 *Communication with Those Charged With Governance* (ASA 260), ASA 265 *Communicating Deficiencies in Internal Control to Those Charged with Governance and Management* (ASA 265) contains information that the auditor may find useful when communicating with Those Charged with Governance. 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 in internal controls identified during the engagement. A significant deficiency in internal control means a deficiency or combination of deficiencies in internal control that, in the 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;
  - Compliance Breaches; and
  - Expected modifications to the auditor's report.
100. The auditor informs those charged with governance of the AFS licensee of those uncorrected misstatements/compliance breaches, other than clearly trivial amounts, aggregated by the auditor during and pertaining to the engagement that were considered to be immaterial, both individually and in the aggregate, to the assurance engagement.



**Conformity with International Pronouncements**

101. There is no equivalent International Standard on Auditing or International Auditing Practice Statement to this GS.

Draft

**APPENDIX 2**

**EXAMPLE AUDIT ENGAGEMENT LETTER**

The following example audit engagement letter is for use as a guide only, in conjunction with the considerations described in GS 003, and will need to be varied according to individual requirements and circumstances.

To [Title of Those Charged with Governance]

Section 989B(3) of the *Corporations Act 2001* (the Corporations Act) requires an Australian Financial Services Licence (AFSL) holder (AFS Licensee) to lodge with ASIC the auditor's report on the AFS licensee together with a profit and loss statement and balance sheet (being the audited financial statements).

The Corporations Act, *Corporations Regulations 2001*, ASIC regulatory documents and ASIC Class Orders determine the scope of the auditor's report. Reference to the auditor's report is also made in the conditions of the AFSL. Currently the required format of the auditor's report is set out in ASIC form FS 71.

This letter sets out in general terms, our understanding of the terms and objectives of our engagement as auditors of the AFSL of [name of company] (the Licensee) pursuant to section 989B(3) of the Corporations Act. This engagement is a separate engagement from our audit [and half year review] appointment[s] under the Corporations Act.

**Scope**

Our reporting will be in a form consistent with the requirements of ASIC form FS 71 which requires:

- Reasonable assurance that the profit and loss statement (Statement of Financial Performance) and balance sheet (Statement of Financial Position) and the notes thereto (financial statements) give a true and fair view of the financial performance and financial position of the AFS licensee for the year ended [date] and comply with all Australian Accounting Standards (covered by a separate engagement letter);
- Reasonable assurance on compliance with specified provisions of Part 7.8 of the Corporations Act (being Divisions 2 to 7, except for section 991A) (including relating to dealing with client money, property and insurance);
- Reasonable assurance on compliance with sections 981B and 982B of the Corporations Act (relating to the control and operation of trust accounts);
- Reasonable assurance that all necessary records, information and explanations for the purpose of the audit report were received;
- A combination of reasonable and limited assurance on compliance with AFSL conditions relating to financial requirements as prescribed by ASIC in regulations and class orders;
- A statement over paragraphs 7, 8 and 9 of ASIC form 70 in relation to receipt of client money, property or loans to which Part 7.8 of the Corporations Act applies; and
- A statement that during the performance of our duties as auditors of the AFS licensee, we have not become aware of any matters referred to in section 990K(2) of the Corporations Act during or since the financial year, that we have not previously reported to ASIC.

### **The responsibilities of the auditor**

ASIC form FS 71 includes a combination of reasonable assurance opinions and limited assurance conclusions on the AFS licensee's compliance with AFSL conditions relating to financial requirements as prescribed by ASIC.

Where we are required to obtain reasonable assurance in relation to ASIC form FS 71, our audit procedures will be conducted in accordance with AUASB Standards, and accordingly will include such tests and procedures as we consider necessary in the circumstances. This will involve an examination of the internal controls used by the AFS licensee to comply with the financial requirements of the AFSL, the specified provisions of Part 7.8 and the control and operation of each account maintained for section 981B or section 982B of the Corporations Act.

Where we are required to obtain limited assurance in relation to ASIC form FS 71, our review procedures are conducted in accordance with Standards on Assurance Engagements. A review consists primarily of inspection of evidence and observation of, and enquiry about, the operation of the procedures and internal control of the financial risk management system and comparison and other such analytical review procedures we consider necessary. A review of this nature does not provide all the evidence that would be required in an audit and provides less assurance than an audit. We will not be performing an audit of the matters subject to review and we will not express an audit opinion on them.

Where we are required to obtain limited assurance in relation to projections, our review procedures will be conducted in accordance with Standards on Assurance Engagements and will be restricted to an examination on a test basis throughout the relevant period to determine whether the AFS licensee had projections in place and may include:

- a review of projections identified on a test basis to ensure that they were materially in accordance with the requirements of the Corporations Act; and
- testing that projections identified on a test basis were mathematically accurate based on the underlying assumptions as documented by the AFS licensee and that these assumptions are not unreasonable.

Our procedures are substantially less in scope than an audit conducted in accordance with AUASB Standards and obtain limited assurance.

Where we are required to obtain limited assurance in relation to the projections required under the cash needs requirements conditions of the AFSL, our review procedures will be conducted in accordance with AUASB Standards on Assurance Engagements in order to state whether anything has come to our attention, which causes us to believe that the AFS licensee did not satisfy the cash needs requirements. Our procedures are substantially less in scope than an audit conducted in accordance with AUASB Standards and obtain limited assurance.

### **Inherent Limitations**

#### *Internal Controls*

Because of the inherent limitations of any internal control structure, it is possible that fraud, errors or non-compliance with laws and regulations may occur and not be detected. We will not audit the overall internal control structure (including procedures that do not relate to the financial requirements) and no opinion will be expressed as to its effectiveness. An audit is not designed to detect all weaknesses in control procedures or all instances of non-compliance with part 7.8 of the Corporations Act as it is not performed continuously throughout the period and the tests performed are on a sample basis having regard to the nature and size of the AFS licensee. Also, projections of any evaluation of the control procedures to future periods are subject to the risk that the procedures may become inadequate because of changes in conditions, or that the degree of compliance with them may deteriorate.

*Projections*

The projections prepared by [Those Charged with Governance] in accordance with the cash needs requirements conditions of the AFSL are based upon the achievement of certain economic, operating and developmental assumptions about future events and actions that have not yet occurred and may not necessarily occur. There is a considerable degree of subjective judgement involved in the preparation of projections. Actual results may vary materially from those projections and the variation may be materially positive or negative.

**Auditor’s obligation to report matters to ASIC**

In accordance with section 990K of the Corporations Act, if during the course of or in relation to our assurance engagement we become aware of a matter referred to in section 990K(2) of the Corporations Act we are required to lodge a written report to ASIC within 7 days.

**Responsibility of the AFS licensee**

The [Title of Those Charged with Governance] of the AFS Licensee are responsible for:

- Establishing and maintaining effective internal control procedures relevant to the preparation and fair presentation of ASIC form FS 70 that is free from material misstatement, including control procedures in relation to compliance with the requirements of Part 7.8 of the Corporations Act, the conditions of the AFSL and the provisions of the financial services laws. These duties are imposed on the AFS licensee by the Corporations Act and the AFSL.
- The preparation and presentation of ASIC Form FS 70, and the information it contains.
- Complying with the requirements of the Corporations Act and the conditions of the AFSL.

**Fees**

We look forward to full cooperation from your staff and we trust that they will make available to us whatever records, documentation and other information we request 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.

As part of our assurance process, we will request from [management, and where appropriate, Those Charged with Governance], written confirmation concerning representations made to us in connection with the assurance process.

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 audit of [Name of the AFS Licensee] as required by Section 989(B) of the Corporations Act.

Yours faithfully,

(signed)

.....

Name and Title

Date

Acknowledged on behalf of [entity] by (signed)

.....

Name and Title

Date

Draft

## **Appendix 2**

(Ref: Para.96)

### **APPENDIX 2**

#### **EXAMPLE MANAGEMENT REPRESENTATION LETTER**

[Client Letterhead]

[Addressee – Auditor]

[Date]

This representation letter is provided in connection with your engagement to report in accordance with section 989B(3) of the *Corporations Act 2001* (the Corporations Act) regarding the Australian Financial Services Licence (“AFSL”) of [Name of the AFS Licensee] (Licence No: [xx]) for the financial year ended [balance date].

We acknowledge our responsibility for the preparation of form FS 70 in accordance with Section 989B of the Corporations Act, the *Corporations Regulations 2001* (the Regulations) and the conditions of the Licensee’s AFSL, effective [date of AFS Licence] and that this responsibility includes designing, implementing and maintaining accounting records and effective internal control to ensure compliance with the conditions of the Licensee’s AFSL and the requirements of Part 7.8 of the Corporations Act.

We confirm, to the best of our knowledge and belief, the following representations:

#### *General*

1. We have made available to you, and your representatives:
  - (a) access to all information of which we are aware that is relevant to the preparation of Australian Securities and Investments Commission (ASIC) form FS 70 such as records, documentation and other matters;
  - (b) additional information that you have requested from us for the purpose of the engagement;
  - (c) unrestricted access to persons within the entity from whom you determined it necessary to obtain evidence; and
  - (d) minutes of all meetings of (*shareholders, directors, and committees of directors*).
2. There:
  - (a) has been no knowledge of any fraud, error or non-compliance with laws and regulations involving management or employees who have a significant role in the internal control structure;
  - (b) has been no knowledge of any fraud, error or non-compliance with laws and regulations that could have a material effect on the either the form FS 70 for [Name of the AFS Licensee], or ongoing compliance with the AFSL; and
  - (c) has been no communications from regulatory agencies concerning non-compliance with, or deficiencies in, financial reporting or compliance practices that could have a material effect on form FS 70 of [Name of the AFS Licensee] or our ongoing ability to comply with financial services laws or conditions of the AFSL.

3. We have disclosed to you:
- (a) all significant facts relating to any frauds or suspected frauds which are known to us that may have affected compliance with the conditions of the Licensees AFSL and the requirements of Part 7.8 of the Corporations Act;
  - (b) the results of our assessment of the risk of non-compliance with the conditions of the Licensee's AFSL and the requirements of Part 7.8 of the Corporations Act as a result of fraud;
  - (c) all information in relation to allegations of fraud, or suspected fraud, affecting ASIC form FS 70 or compliance with the conditions of the Licensee's AFSL and the requirements of Part 7.8 of the Corporations Act communicated by employees, former employees or others;
  - (d) known actual or possible non-compliance with laws or regulations, that could have a material effect on ASIC form FS 70 in the event of non-compliance; and
  - (e) all known actual or possible litigation and claims whose effects should be considered when preparing ASIC form FS 70 and compliance with the conditions of the Licensee's AFSL and the requirement of Part 7.8 of the Corporations Act.
4. We acknowledge our responsibility for the design and implementation of internal controls to detect fraud and error.
5. We acknowledge our responsibility for the preparation and presentation of a profit and loss statement, balance sheet and notes thereto in accordance with applicable Australian Accounting Standards and other mandatory professional reporting requirements in Australia, the Corporations Act and the appropriate disclosures of all information required by statute.

*ASIC Form FS 70*

6. We confirm that all transactions have been properly recorded and reflected in the accounting records underlying form FS 70 and that we have in place adequate systems of accounting procedures and internal control to ensure that all transactions are recorded and that the recorded transactions are valid, accurate, authorised, classified and promptly recorded so as to facilitate the preparation of reliable financial information referred to in form FS 70.
7. We confirm that form FS 70, to which form FS 71 relates, has been prepared so as to be consistent with [Name AFS Licensee]'s audited financial report and it has been properly drawn up so as to provide the information required by directions issued by ASIC under the Corporations Act and the Corporations Regulations.
8. We confirm that all material and/or contentious issues which management or the directors have discussed in the course of preparing form FS 70 and any non-compliance with the conditions of the Licensee's AFSL and the requirements of Part 7.8 of the Corporations Act, and the resolution of such issues have been discussed with you.
9. We confirm that the statements made in respect of paragraphs 7, 8 and 9 on FS 70 are correct.

*Part 7.8 of the Corporations Act 2001*

10. There has been no matter during or since the end of the year/period ended [selected date] which has adversely affected, is adversely affecting or may adversely affect our ability to meet our obligations as a AFS licensee or constitutes a contravention of :
- (a) a provision of Subdivision A or B of Division 2 of Part 7.8 of the Corporations Act (or a provision of regulations made for the purposes of such a provision); or

- (b) a provision of Division 3 of Part 7.8 of the Corporations Act (or a provision of regulations made for the purposes of such a provision); or
  - (c) a provision of Subdivision B or C of Division 6 of the Part 7.8 of the Corporations Act (or a provision of regulations made for the purposes of such a provision); or
  - (d) a condition of the licence.
11. We have designed and operated controls effectively to ensure that we comply with Divisions 2, 3, 4, 4A, 5, 6 and 7 of Part 7.8 of the Corporations Act (other than section 991A).
12. We have operated and controlled each account required by sections 981B and 982B of the Corporations Act in accordance with those sections.

*Financial Requirements*

13. We have complied with all the financial requirements under the Licence throughout the year/period.
14. We acknowledge that we were a body regulated by the Australian Prudential Regulation Authority (“APRA”) / participant in the market conducted by the ASX Limited (“ASX”) or Chi-X / participant in the market conducted by the Australian Securities Exchange Limited (“ASX 24”) that restricted its financial services business to participating in the market and incidental business / participant in the licensed clearing and settlement facility operated by ASX Clear Pty Limited / participant in the licensed clearing and settlement facility operated by ASX Clear (Futures) Pty Limited and restricted its financial services business to participating in the licensed clearing and settlement facility and incidental business for the year ended [balance date]. ***[delete if AFS licensee is not APRA regulated or a market or clearing participant]***
15. We have maintained adequate risk management systems throughout the year/period to manage the risk of having insufficient financial resources to comply with the conditions of the Licence. ***[delete if APRA-regulated]***
16. We acknowledge our responsibility for the preparation of cash flow projections and the assumptions underpinning those projections, and confirm that the assumptions adopted for the projections were reasonable/the basis for the selection of assumptions to meet the requirements for the projections adopted was reasonable. ***[delete as applicable depending on whether the licensee is complying with Option 1 or Option 2]***
17. We confirm that we have had our cash flow approved by [those charged with governance]; and have updated our projection of cash flows in line with the requirements of ASIC regulatory guide RG 166. ***[delete if AFS licensee is not subject to tailored cash requirements]***
18. We confirm that we have access as needed to enough financial resources to meet our liabilities over the next 3/12 months, including any additional liabilities that we project we will incur during that term/we might incur during that term. ***[delete as applicable depending on whether the AFS licensee is complying with tailored cash requirements, Option 1 or Option 2]***In relation to forecast financial information provided to you for the purpose of your report (in particular the cash needs requirements prescribed by Option 1 or Option 2 or the tailored cash need requirements as referred to in your AFSL and ASIC form FS 71), it is confirmed, to the best of our knowledge and belief, that:
- (a) the financial position and operating results for the forecast period reflect the best judgement of our directors and management based on expected future market conditions and the likely course of action to be taken;
  - (b) the accounting principles used in the preparation of the forecast data are consistent with those used in our historical financial statements and are the same as those



expected to be used in the eventual preparation of the historical financial statements come the end of the forecast period;

- (c) there are no contingent liabilities, unusual contractual obligations or substantial commitments which would materially affect the financial forecast except as otherwise specifically disclosed to you;
- (d) the key assumptions have been consistently applied during the forecast period; and
- (e) no factors that may be relevant have been omitted.

*Uncorrected Misstatements and Non Compliance Identified*

- 19. We acknowledge that you have advised management of identified uncorrected misstatements, instances of non-compliance with the conditions of the Licensee's AFSL and the requirements of Part 7.8 of the Corporations Act; and identified weaknesses in the design of the internal controls that you became aware of as a result of your audit and review procedures.
- 20. We believe the effects of uncorrected misstatements, instances of non-compliance with the conditions of the Licensee's AFSL and the requirements of Part 7.8 of the Corporations Act; and weaknesses in the design of internal controls summarised [in Appendix [X]/below] pertaining to the year ended [balance date] (including the effects of prior year issues impacting the current year) are both individually, and in aggregate, immaterial or adequately reported ASIC.

*Subsequent Events*

- 21. No events have occurred subsequent to [balance date] that would require adjustment to form FS 70 at that date.

*Additional Matters*

- 22. We have reported any significant breaches to ASIC as required under:
  - (a) section 912D of the Corporations Act; and
  - (b) section 601FC(1)(l) of the Corporations Act [*delete if licensee is not a responsible entity of a managed investment scheme*]

and have provided you with details of all breaches, reported and unreported, of the Licence or the Corporations Act that occurred during or since the end of the year/period.

- 23. We understand that your engagement has resulted in a combination of reasonable assurance opinions and limited assurance conclusions. Where you were required to obtain reasonable assurance we understand that your audit was conducted in accordance with AUASB Standards and was designed primarily for the purpose of expressing an opinion in relation to ASIC form FS 71 and that your audit procedures were limited to those you considered necessary in the circumstances. In addition, we understand that the limited assurance conclusions were also conducted in accordance with AUASB Standards and involved review procedures. These procedures result in you obtaining less assurance than that provided by an audit. For these conclusions you have not performed an audit and accordingly do not express an opinion on them.
- 24. [Include any additional matters relevant to the engagement]

Yours faithfully

Name of signing officer and title

**Appendix 3**

(Ref: Para.19, 22 )

**APPENDIX 3**

**SUMMARY OF FINANCIAL REQUIREMENTS APPLICABLE TO CERTAIN AFS LICENSEES**

This table summarises and provides the regulatory references for certain financial and assurance requirements applicable to all non-exempt AFS Licensees, Responsible Entities, Operators of IDPS and Retail OTC derivative issuers. This appendix may not be a complete summary of all legislative requirements. Practitioners are advised to refer to the current legislation and ASIC Regulatory Guides in place.

	<b>Base Level requirements applicable to all non-exempt AFS Licensees</b>	<b>Responsible Entities and operators of IDPSs</b>	<b>Retail OTC derivative issuers</b>	<b>Custodial or depository services</b>
<b>Regulatory References</b>	<ul style="list-style-type: none"> <li>• RG 166 Section B</li> <li>• ASIC PF 209 paragraph 13</li> </ul>	<ul style="list-style-type: none"> <li>• RG 166 Appendix 2 and 3</li> <li>• ASIC Class Order CO 13/760</li> </ul>	<ul style="list-style-type: none"> <li>• RG 166 Appendix 8</li> <li>• ASIC Class Order CO 12/752</li> </ul>	<ul style="list-style-type: none"> <li>• RG 166 Appendix 4</li> <li>• ASIC Class Order CO 13/761</li> </ul>
<b>Solvency and positive net assets</b>	<ul style="list-style-type: none"> <li>• Ability to pay debts when due and payable</li> <li>• Total assets exceeding total liabilities (unless using adjusted assets and liabilities [RG 166 Section E]</li> <li>• [RG 166.32 – RG 166.34]</li> <li>• [ASIC PF 209 para 13]</li> </ul>	<ul style="list-style-type: none"> <li>• Base level solvency and positive net assets</li> </ul>	<ul style="list-style-type: none"> <li>• Base level solvency and positive net assets</li> </ul>	<ul style="list-style-type: none"> <li>• Base level solvency and positive net assets</li> </ul>
<b>Cash needs</b>	<ul style="list-style-type: none"> <li>• Not applicable where a tailored cash needs requirement applies</li> <li>• Option 1 [RG 166.40- RG 166.44]</li> <li>• Option 2 [RG 166.45- RG 166.47]</li> <li>• Option 3 [RG 166.50]</li> </ul>	<ul style="list-style-type: none"> <li>• Tailored cash need requirement [RG 166.204- RG 166.205]; [RG 166.237 – RG 166.238]</li> <li>• At least 12 month cash flow projection</li> <li>• Documentation of calculations and assumptions</li> </ul>	<ul style="list-style-type: none"> <li>• Tailored cash need requirement [RG 166.314 – RG 166.318]</li> <li>• At least 12 month rolling cash flow projection</li> <li>• Documentation of calculations and assumptions</li> <li>• Board approval of the cash</li> </ul>	<ul style="list-style-type: none"> <li>• Tailored cash need requirement [RG 166.263- RG 166.264]</li> <li>• At least 12 month cash flow projection</li> <li>• Documentation of calculations and assumptions</li> </ul>

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	<ul style="list-style-type: none"> <li>Option 4 [RG 166.51]</li> <li>Option 5 [ RG 166.52]</li> <li>[ASIC PF 209 para 13]</li> </ul>	<ul style="list-style-type: none"> <li>Board approval of the cash flow projections at least quarterly</li> </ul>	<p>flow projections</p>	<ul style="list-style-type: none"> <li>Cash flow projections approved at least quarterly</li> </ul>
<b>NTA</b>	<ul style="list-style-type: none"> <li>N/A</li> </ul>	<ul style="list-style-type: none"> <li>[RG 166.209 – RG 166.235]; [RG 166.242-RG 166.261]</li> <li>If requirements related to custody are satisfied or licensee is an IDPS operator, the greater of: <ul style="list-style-type: none"> <li>\$150,000 or</li> <li>0.5% of average value of scheme and IDPS property up to \$5 million or</li> <li>10% of average RE and IDPS revenue</li> </ul> </li> <li>If requirements related to custody are not satisfied or licensee performs custodial functions as an IDPS operator, the greater of: <ul style="list-style-type: none"> <li>\$10 million or</li> <li>10% of average RE and IDPS revenue</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>RG 166.322 – RG 166.332</li> <li>Greater of: <ul style="list-style-type: none"> <li>\$1,000,000 or</li> <li>10% of average revenue</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>[RG 166.269 – RG 166.289]</li> <li>Other than incidental<sup>15</sup> providers (satisfy requirements for custodian) the greater of: <ul style="list-style-type: none"> <li>\$10million or</li> <li>10% of average revenue</li> </ul> </li> <li>For incidental providers: <ul style="list-style-type: none"> <li>If all assets are held by another complying custodian or eligible custodian – no NTA requirement; otherwise the greater of: <ul style="list-style-type: none"> <li>\$150,000 or</li> <li>10% of average revenue</li> </ul> </li> </ul> </li> </ul>
<b>Liquidity</b>	<ul style="list-style-type: none"> <li>N/A</li> </ul>	<ul style="list-style-type: none"> <li>[RG 166.212; RG 166.244]</li> <li>Greater of \$150,000 or 50% of NTA in cash and cash equivalent; and</li> </ul>	<ul style="list-style-type: none"> <li>[RG 166.323]</li> <li>50% of NTA in cash or cash equivalents; and</li> <li>50% of NTA in liquid assets.</li> </ul>	<ul style="list-style-type: none"> <li>[RG 166.270]</li> <li>At least 50% of NTA in cash and cash equivalent; and</li> </ul>

<sup>15</sup> Incidental provider is defined in RG 166.173.

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		<ul style="list-style-type: none"> <li>At least 100% of NTA in liquid assets</li> </ul>		<ul style="list-style-type: none"> <li>At least 100% of NTA in liquid assets</li> </ul>
<b>Audit</b>	<ul style="list-style-type: none"> <li>RA: Financial requirement;</li> <li>RA/LA: Cash needs requirement</li> <li>LA: s912A(1)(h)</li> <li>[RG 166.62-RG 166.68]</li> <li>[PF 209 para 28(d)]</li> </ul>	<ul style="list-style-type: none"> <li>Combination RA and LA</li> <li>Tailored audit requirements [RG 166.206 – RG 166.208]; [RG 166.239 – RG 166.241]</li> </ul>	<ul style="list-style-type: none"> <li>Combination RA and LA</li> <li>Tailored audit requirements [RG 166.319 – RG 166.321]</li> </ul>	<ul style="list-style-type: none"> <li>Combination RA and LA</li> <li>Tailored audit requirements [RG 166.265 – RG 166.67]</li> </ul>

RA: Reasonable assurance  
 LA: Limited assurance

Draft

## **APPENDIX 4**

### **TAILORED CASH REQUIREMENTS**

This appendix *summarises* the tailored cash requirements needs for Responsible Entities, Operators of Investor Directed Portfolio Services (IDPS), Custodial or Depository Service Providers and retail OTC Derivative Issuers. A responsible entity authorised to operate a managed investment scheme and IDPS operators are required to comply with the financial requirements as set out in RG 166 Appendix 2 and 3, and ASIC Class Order CO 13/760. The financial requirements for custodial or depository service providers are set out in RG 166 Appendix 4 and ASIC Class Order CO 13/761. The financial requirements for retail OTC derivative issuers are set out in RG 166 Appendix 8 and ASIC Class Order CO 12/752. This appendix may not be a complete summary of all legislative requirements. Practitioners are advised to refer to the current legislation and ASIC Regulatory Guides in place.

To meet the cash needs requirement, the licensee is required to:

- (i) prepare a projection of the licensee's cash flows over at least the next 12 months (for retail OTC derivative issuers this is required to be done quarterly in March, June, September and December) based on the licensee's reasonable estimate of what is likely to happen over this period (retail OTC derivative issuers – revenue and expenses); and
- (ii) have the projection approved in writing at least quarterly by the licensee's directors (unless the licensee is a retail OTC derivative issuer or custodial or depository service provider who may then have the projection approved by partners or trustees of the licensee if the licensee is a partnership or a trust, or a person if the licensee is a natural person) as satisfying the requirements of paragraph (i); and
- (iii) document the calculations and assumptions used in preparing the projection, and describe in writing why the assumptions are appropriate; and
- (iv) update the projection of the licensee's cash flows if:
  - the projection ceases to cover at least the next 12 months (not a requirement for retail OTC derivative issuers); or
  - there is reason to suspect that an updated projection would differ materially from the current projection (not a requirement for retail OTC derivative issuers) or show that the licensee was not meeting the requirements in subparagraphs (v) below; and
- (v) document whether (retail OTC derivative issuers require a certification in writing by the persons referred to in (ii) above), based on the projection of the licensee's cash flows, the licensee:
  - will have access when needed to enough financial resources to meet its liabilities over the projected term of at least the next 12 months; and
  - will hold at all times during the period to which the projection relates in cash or cash equivalents, an amount equal to or greater than the current amount the licensee is required to hold in cash or cash equivalents under the licensee's liquidity requirement; and
- (vi) make the projections available to ASIC on request (requirement for retail OTC derivative issuers only).

**Appendix 5**

(Ref: Para.22(d))

**APPENDIX 5**

**TAILORED ASSURANCE REQUIREMENTS**

This appendix summarises the tailored audit requirements applicable for Responsible Entities, Operators of Investor Directed Portfolio Services (IDPS), Custodial or Depository Service Providers and retail OTC Derivative Issuers. A responsible entity authorised to operate a managed investment scheme and IDPS operators are required to comply with the audit requirements as set out in RG 166 Appendix 2 and 3, and ASIC Class Order CO 13/760. The audit requirements for custodial or depository service providers are set out in RG 166 Appendix 4 and ASIC Class Order CO 13/761. The audit requirements for retail OTC derivative issuers are set out in RG 166 Appendix 8 and ASIC Class Order CO 12/752. This appendix may not be a complete summary of all legislative requirements. Practitioners are advised to refer to the current legislation and ASIC Regulatory Guides in place.

- (i) If the licensee is a responsible entity, operator of an IDPS, a custodial or depository service provider then ASIC requires the following:
- Reasonable assurance that the licensee:
- ◇ complied with the requirement to have the projection approved in writing at least quarterly by the directors/partners/person and that the licensee has met the NTA and liquidity requirement of the licence, and any other financial requirements in conditions on its licence; and
  - ◇ had, at all times, a projection over at least the next 12 months that purports to, and on appears on its face to be based on the licensee's reasonable estimate of what is likely to happen over this period; and
  - ◇ correctly calculated the projection on the basis of the assumptions the licensee used for the projection; and
- (ii) If the licensee is a responsible entity or operator of an IDPS, a custodial or depository service provider then ASIC requires the following:
- Limited assurance that the licensee:
- ◇ had adequate systems for managing the risk of having insufficient financial resources to meet the NTA requirement, cash/cash equivalent, and liquid asset holding requirement, and any other financial requirements in conditions on its licence; and
  - ◇ did not fail to document the calculations and assumptions used in preparing the projection and describe in writing why the assumptions are appropriate; and
  - ◇ will have access when needed to enough financial resources to meet their liabilities over the projected term of at least the next 12 months; and
  - ◇ will hold at all times during the period to which the projection relates, in cash/cash equivalents and liquid assets, an amount equal to or greater than the current amount the licensee is required to hold in cash or cash equivalents; and
  - ◇ adopted assumptions for its projection that were not unreasonable; or

- ◇ (if the licensee complies with the NTA requirement for incidental providers) satisfied the definition of incidental provider.
- (iii) If the licensee is a retail OTC derivative issuer then ASIC requires the following:
- Reasonable assurance that the licensee:
- ◇ complied with the NTA and liquidity requirements of the licence and other financial requirements in conditions on its licence; and
  - ◇ had at all times a projection that purports to, and appears on its face to, comply with the requirement to prepare in each March, June, September and December, a projection of the licensee's cash flows over at least the next 12 months based on the licensee's reasonable estimate of revenues and expenses over this period; and
  - ◇ correctly calculated the projection on the basis of the assumptions the licensee adopted for the projection; and
- Limited assurance that the licensee:
- ◇ satisfied s912A(1)(h) of the *Corporations Act 2001* for managing the risk of having insufficient financial resources to meet the NTA and liquidity requirement of the licensee and any other financial requirements in conditions on its licence; and
  - ◇ adopted assumptions for its projection that were not inappropriate; and
  - ◇ had their projections approved in writing by their directors/partners/person as being based on the licensee's reasonable estimate of revenues and expenses over the period; and
  - ◇ documented the calculations and assumptions used in preparing the projection, and described in writing why the assumptions are appropriate; and
  - ◇ updates the cash flow projections if there is reason to suspect that an updated projection would show that the licensee :
    - will not have access when needed to enough financial resources to meet its liabilities over the projected term of at least the next 12 months; and
    - will hold at all times during the period to which the projection relates in cash or cash equivalents, an amount equal to or greater than the current amount the licensee is required to hold in cash or cash equivalents.

**Appendix 6**

(Ref: Para.19(b) )

**APPENDIX 6**

**CASH AND ASSURANCE REQUIREMENTS**

This appendix summarises the cash and assurance requirements, that are detailed in ASIC Pro Forma 209, for licensees that are not regulated by APRA or are not market or clearing participants and are not subject to tailored cash and assurance requirements as outlined in Appendix 4 and 5. AFS Licensees that are not APRA regulated or market participants are also subject to the requirements for reasonable assurance in respect of other relevant financial conditions on their licence which may be applicable based on the nature of their business. This appendix may not be a complete summary of all legislative requirements. Practitioners are advised to refer to the current legislation and ASIC Regulatory Guides in place.

- (i) If the licensee is relying on satisfying the cash needs requirement by Option 1 or Option 2, then ASIC requires the following:
- Reasonable assurance that the licensee had at all times a projection (covering at least the following 3 months) that purports to, and appears on its face to comply with, paragraph (a) of the definition of Option 1 or paragraph (a) of the definition of Option 2 (depending on which option the licensee purports to be complying with); and
  - Reasonable assurance that the licensee has correctly calculated the projections on the basis of the assumptions the licensee adopted for the projections described above; and
  - Limited assurance that the licensee is managing the risk of having insufficient financial resources to comply with the conditions of the licence; and
  - Limited assurance over the cash needs requirement using either Option 1 or Option 2 except for paragraphs (a), (c) and (e) of the definition of Option 1 or paragraphs (a) and (c) of the definition of Option 2; and
  - If the licensee relied on Option 1, limited assurance that the assumptions the licensee adopted for its projection were not unreasonable; or
  - If the licensee relied on Option 2, limited assurance that the basis for the selection of assumptions to meet the requirements for the projection adopted was not unreasonable; or
- (ii) If the licensee is relying on satisfying the cash needs requirement with a financial commitment by an Australian ADI or comparable foreign institution (Option 3), then ASIC requires:
- Reasonable assurance that the licensee has obtained from an Australian ADI or a foreign deposit-taking institution approved in writing by ASIC as an eligible provider an enforceable and unqualified commitment to pay on demand from time to time an unlimited amount to the licensee, or the amount for which the licensee is liable to its creditors at the time of demand to the licensee's creditors or a trustee for the licensee's creditors; and
  - Limited assurance that the licensee is managing the risk of having insufficient financial resources to comply with the conditions of the licence; and



- Limited assurance that the basis for the selection of the assumptions adopted was not unreasonable; or
- (iii) If the licensee is relying on satisfying the cash needs requirement by relying on licence condition 13(c)(iv) (Option 4), then ASIC requires:
- Reasonable assurance that the licensee is a subsidiary of an Australian ADI or a corporation approved by ASIC in writing; and
  - Reasonable assurance that a responsible officer of the licensee has documented that the officer has the reasonable expectation for at least the following three month period together with the reasons for forming the expectation, the contingencies for which the licensee considers it is reasonable to plan, the assumptions made concerning the contingencies and the basis for selecting those assumptions; and
  - Limited assurance that the licensee is managing the risk of having insufficient financial resources to comply with the conditions of the licence; and
  - Limited assurance that the basis for the selection of the assumptions adopted was not unreasonable; or
- (iv) If the licensee is relying on satisfying the cash needs requirement by relying on licence condition 13(c)(v) (Option 5), then ASIC requires:
- Reasonable assurance that the cash flows of the licensee and each of its related bodies corporate, other than a body regulated by APRA (“licensee group”), are managed on a consolidated basis and there is a body corporate within the licensee group of which all members of the licensee group are subsidiaries that is not a body regulated by APRA (“parent entity”); and
  - If the licensee is relying on Alternative A, reasonable assurance that the parent entity has provided an enforceable and unqualified commitment to pay on demand from time to time an unlimited amount to the licensee or to meet the licensee’s liabilities; or
  - If the licensee is relying on Alternative B:
    - Limited assurance that the licensee is managing the risk of having insufficient financial resources to comply with the conditions of the licence; and
    - Limited assurance that the basis for the selection of the assumptions adopted was not unreasonable.
  - In addition to the above, under subparagraph 13(c)(v)(D), a report by the parent entity’s auditor is given to ASIC with the licensee’s annual audit report under condition 28 of its licence, with respect to compliance by the parent entity with Option 1 or Option 2 as they would apply in accordance with subparagraph (c) reflecting the report that would be required from the auditor of a licensee, for that period purporting to comply with Option 1 or 2.