

## AGENDA PAPER

**Item Number:** 10  
**Date of Meeting:** 28 August 2020  
**Subject:** Update on Audit Standard Setting and Regulation

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Action required     For discussion     For noting     For information

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### Purpose

To provide the Board with an update on recent developments relating to Audit Standard Setting and Regulation.

### Background

Over the past few years, there has been an increased focus on the independence of auditors, with calls for more transparency in the accounting sector and reforms to how the accounting profession is regulated. APESB Technical Staff have been monitoring both local and international developments that relate to audit standard-setting and regulation and updating the Board as required.

### Matters for Consideration

Since the last Board Meeting, there have been three key developments for the Board to note:

- Addressing the recommendations from the interim report of the PJC Inquiry into audit regulation in Australia;
- The Monitoring Group's final report on proposed reforms to the international audit and ethics standard-setting system; and
- The FRC UK is setting operational separation principles for the Big 4 firms in the UK.

#### 1) **PJC Inquiry into Audit Regulation in Australia**

On 1 August 2019, an inquiry into the regulation of the auditing profession in Australia was referred to the Parliamentary Joint Committee on Corporations and Financial Services (PJC Inquiry).

The PJC Inquiry issued an [interim report](#) in late February 2020, which included ten preliminary recommendations, of which three were specifically relevant to the APESB (Recommendation 3, 4 and 5). With the recent extension to the Inquiry's timeline due to the COVID-19 pandemic. The final report of the PJC Inquiry is not expected until early December 2020, but at this stage, it is likely the interim recommendations will be included in the final report. The PJC has also scheduled further public hearings on the 5<sup>th</sup> & 13<sup>th</sup> of November 2020 in Canberra.

APESB's CEO, Mr Channa Wijesinghe, has been attending a weekly stakeholder meeting convened by the Financial Reporting Council (FRC) to consider how to best address the PJC inquiry recommendations.

APESB's standards are likely to be impacted by recommendation number three, which suggests the development of defined categories and associated fee disclosure requirements concerning audit and non-audit services, and development of a list of non-audit services that audit firms are explicitly prohibited from providing to an audited entity. APESB has recently issued the [APES 110 Code Prohibitions Publication](#) to provide stakeholders with a summary of prohibitions in the existing APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code).

In addition, there are two significant global International Ethics Standards Board for Accountants (IESBA) projects dealing with audit fees and non-assurance services that are expected to be finalised by December 2020. It is expected that there will be a significant narrowing of other services an auditor can provide to audit clients as well as the nature of those services. The fees project will also drive fee disclosures of the auditor. In due course, the approved global independence standards will be incorporated by APESB in the Australian Code.

APESB has considered recommendation 5, which suggests the Code be amended to include a safeguard that no audit partner can be incentivised, through remuneration advancement or any other means or practice, for selling non-audit services to an audited entity. If this is a final recommendation of the PJC, APESB will take action to propose an amendment to the Code, which will need to go through the normal APESB public due process before its adoption.

## **2) Monitoring Group**

The Monitoring Group is a group of international financial institutions and regulatory bodies committed to advancing the public interest in areas related to international audit standard-setting and audit quality. The members of the Monitoring Group are the Basel Committee on Banking Supervision, European Commission, Financial Stability Board, International Association of Insurance Supervisors, International Forum of Independent Audit Regulators, International Organization of Securities Commissions, and the World Bank.

In November 2017, the Monitoring Group issued a public consultation paper on the governance, accountability, and oversight of the international audit standard-setting process. The proposed reforms suggested changes to the structure of the international boards (creation of a single board for setting audit and ethics standards for auditors), the focus of the Board, the board composition, board appointments and remuneration, and the funding model.

After a comprehensive stakeholder engagement process, the Monitoring Group released its final report, *Strengthening the International Audit and Ethics Standard-Setting System* in July 2020.

APESB Technical Staff have reviewed the recommendations in the final report against the concerns it raised to the Monitoring Group in [APESB's submission](#) made in February 2018. Technical Staff are pleased to note the following recommendations which address many of the concerns APESB raised:

- Two separate Boards will address ethics and auditing, with no change to the mandate of either the International Auditing and Assurance Standards Board (IAASB) or the IESBA;
- Balancing priorities to include the perspective of small and medium enterprises when developing standards;
- Removal of suggested veto power for the Public Interest Oversight Board (PIOB);
- The adoption of a two-thirds majority for approving the issuance of due process documents such as exposure drafts or final standards;
- The International Federation of Accountants (IFAC) to maintain its responsibility of promoting global adoption of international standards; and
- Expansion of each Board's technical staff to reduce reliance on technical advisors seconded to the Boards.

Refer to Agenda Item 10 (a) for the Monitoring Group final report and the full list of recommendations.

### **3) FRC Principles for Operational Separation**

There have been several reviews conducted in the UK on audit, including:

- The Independent Review into the Quality and Effectiveness of Audit (the Brydon review) (refer to [Agenda Item 6 of BM 98 \(Mar 2020\)](#) for the summarised list of recommendations);
- the Competition and Market Authority's (CMA) [audit market study](#) (which called for the operational separation of the audit function of the major accounting firms);
- the Independent Review into the FRC's role and effectiveness in the UK regulatory environment (the Kingman review which resulted in the wholesale replacement of the current FRC UK, in both its function and structure, with a new Audit, Reporting and Governance Authority); and
- the UK Government - Business, Energy, and Industrial Strategy (BEIS) Future of Audit report (summarised at [Agenda Item 5\(c\) of BM 93 \(June 2019\)](#)).

As part of the action being taken to address these reviews, the FRC UK released in June 2020 [a list of principles](#) for the operational separation of the auditing arm of Big 4 firms from the rest of the firm. The objective of the reform is to ensure that audit practices are focused above all on delivery of high-quality audits in the public interest and do not rely on persistent cross-subsidy from the rest of the firm.

The FRC is seeking agreement from the Big 4 firms to implement operational separation of their audit practices on this basis by 30 June 2024 at the latest.

At this stage, it is now known whether this change in the UK will impact the Australian operations of the Big 4 firms. APESB Technical Staff will continue to monitor these developments.

## **Recommendation**

The Board note the update on local and international developments relating to Audit Standard Setting and Regulation.

## **Materials Presented**

Agenda Item10 (a)      Monitoring Group final report

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