Auditor Independence

PROFESSOR IAN RAMSAY’S report on auditor independence has created much interest and discussion. The report will form the basis of government action. The Institute provided its views on the Ramsay Report in a recent submission.

In the wake of topical public debate following the high profile collapses of HIH, One.Tel, Ansett and Enron, the issue of auditor independence is critical to upholding investor and market confidence in the auditing function, the financial reporting system and the sharemarket.

The Institute has made a submission supporting the Independence of Australian Company Auditors report (known as the Ramsay Report) recommendations.

In addressing the key issues of regulating the auditing profession, safeguarding auditor independence and audit effectiveness, the Institute agreed with the Report’s mixed approach of co-regulation between the regulators and the professional accounting bodies.

However, to specifically oversee and discipline the auditing profession, the Institute stated its preference for a primary framework of self-regulation by professional bodies, accounting and audit standards, professional ethics and best practice guidelines in line with international best practice.

In line with the ICAA and CPA Australia submissions, the Institute endorsed the Report’s recommendation for mandatory independent audit committees for listed companies as a means of improving their corporate governance, risk management and financial reporting obligations. As the recent ASIC survey showed, many major companies already have audit committees in place to ensure compliance with legal and ethical obligations.

The Institute would however have reservations about imposing any prescriptive regulatory measures that would place an inappropriate or unnecessary compliance burden on small listed companies or on forcing compulsory (and costly) compliance procedures appropriate for large companies onto small companies.

The Institute believes that further thought must also be given to what would be the most appropriate and effective method (ASX, ASIC or legislation)

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of setting up and enforcing the mandatory audit committee requirement in practice.

As auditor independence in fact and in appearance is crucial to maintaining confidence in the capital markets and financial reporting system, the Institute would agree to the legislative statement of a specific requirement for auditors to be independent.

The Institute supported the recommendation for mandatory rotation of the audit partner from an audit firm as a sound measure to reduce the potential for compromised audits. However, the Institute stated that it would be reluctant to support extending this auditor rotation concept to requiring regular rotation of the actual audit firm.

The introduction of detailed disclosure of both audit and non-audit services provided to a company by the same firm would be favourable, as this would enhance increased transparency for shareholders.

In examining auditor independence and adopting any of the Ramsay Report recommendations, the Government needs to find a practical balance in effectively integrating the existing co-regulatory regime and any proposed policy or structural reforms.

It also needs to take into account the increasingly global nature of Australian companies and their operations, the role of auditors in the wider market context and the need for continuing education and competency training of auditors.

There is a need to look not just at the audit process, but also at enhancing auditor competence and audit performance measures and at the fundamental outcomes for the auditing profession, company reporting and disclosure and market integrity.

The Ramsay Report recommendations were well received by the Government, the Opposition parties, the major accounting bodies and by the profession generally. The Institute eagerly awaits the Government’s review of public submissions and the release of its draft policy.

Submission on investment property (ED 103)

In a brief submission to the Australian Accounting Standards Board (AASB) on the ED 103 Exposure Draft on Investment Property (and consequential amendments to AASB 1021/AAS 4 and AASB 1041), the Institute supported the proposed standard as a means of creating more certainty in this specialised area.

The Institute’s submission stated a preference for the fair value method option (over the cost value method) so as to ensure consistency of accounting treatment at the national and international levels and within asset classes.

The Institute believes that neither party to a property transaction should be given the option of using an alternative method of recognition, as the granting of alternative treatments in any financial reporting would substantially reduce comparability.