



ASIC
Australian Securities &
Investments Commission

Committee	Parliamentary Joint Committee on Corporations and Financial Services
Inquiry	Oversight of ASIC, the Takeovers Panel and the Corporations Legislation No.1 of the 46th Parliament
Question No.	006.1
Date	26 November 2021
Topic	General Brief on ASIC's Audit Inspection Program
Reference	Spoken, 26 November 2021, Hansard page 13 and 14
Committee member	Senator O'Neill

Question

Senator O'NEILL: Thank you. My questions go to the comments in response to Senator Georganas's question around auditing. I have a very keen interest in it because I understand how critical it is. Like many Australians, I didn't know that much about audit before I came on this committee and started to find out more about it. The history of it is very important. Its emergence happened as a vital way to make sure accurate information is provided to the market so people can make informed decisions. So that's it in a nutshell: they are truth tellers about numerical facts that influence decisions on where people invest their money. I figured that out eventually. So, with regard to audit, it really matters that audit quality is high. There have been significant concerns and this committee wrote an extensive report about those concerns. ASIC responded by providing further oversight of the audit profession. and has published a condensed version of an assessment—when you go to the doctor to get a check-up, we get an annual check-up on what you think is going on.

With regard to the resourcing of ASIC, and the time and capacity required to undertake a sufficient review—and I have had questions answered before that tell me it's risk based assessment—I want to know the scale of investigation of those major audit companies. As I understand, it's reduced down to a percentage of value points. Is there equitable investigation of each of the different auditing companies? How is that quality managed, and what assurance can you give me that the skill level and quality of that investigation is sufficiently robust to provide us with such a significant figure that it will impact people's sense of assurance about the audit quality of Australia? There are a range of questions in there, and I'm happy for you to give me your best response.

Mr Day: Could I ask for clarification on what you mean by 'equitable'?

Senator O'NEILL: I wonder if each of the entities is investigated to the same degree. How many do you do in each of those? Whether you have a large sample or a small sample is significantly going to impact the outcome that you will find. I want to understand the shape of that inquiry, the quality of the inquiry and the investment of time, energy and expertise—and at what level—in that significant inquiry that occurs.

Mr Day: I'd probably start off at least at an organisational level. I expect that Commissioner Hughes and Commissioner Armour may want to add detail. We have a dedicated team in ASIC called the Financial Reporting and Audit Team. It's led by our chief accountant. It has dedicated senior professionals who do constant reviews of all the large firms, effectively, for the very reasons you've identified as being important and which ASIC acknowledges. That dedication shows how seriously we take that. In terms of quality, they're not the only auditors within the industry but they certainly take up a large part of the market. In fact, they become some of the most important parts of the market because of the nature of the organisations

they audit, which people rely on for the reasons you've said. So on that basis I would say it is equitable and consistent in the way we look at those. Within that, depending on the issue—

Senator O'NEILL: To be clear, you talked about the staffing and then you jumped to the number. Can I ask about the staffing? I've been profoundly impressed by the work of Mr McPhee as the auditor here and Mr Hehir as the Auditor-General. That sort of skill level seems to me to be the skill level that you'd want to be at to be able to make this discernment of the auditors that are managing the whole ecosystem.

Mr Day: Yes.

Senator O'NEILL: How many staff do you have working on this? How would their skill and depth of knowledge compare with those two luminaries in terms of who goes out and does the work, and how much time, money and skill you invest in it? I want to understand the shape of what you're doing.

Mr Day: I don't know that I can answer that. These are highly proficient auditors with backgrounds in this space. Mr Niven, who is our chief accountant, is well respected in the area and has been in the industry for a long time—

Senator O'NEILL: And he's given us excellent evidence in the past.

Mr Day: I thank you for supporting me in what I've said. I'm sure Mr Niven will be pleased as well. In terms of quality, that's all I can say. I can't put them at luminary status, as you have put the others, but I can certainly say they are well qualified and well drilled in these spaces.

Senator O'NEILL: That's a general response. I might just indicate that, on notice, I would prefer a more robust response.

Mr Day: I understand.

Senator O'NEILL: I basically want to see if there's any experience. I want you attest to and for me to be able to discern the depth and richness of the experience that people bring to it. I want to be sure it's not junior people who are allocated this task, and I want to be sure that there is no curtailment of their capacity to do their work if they find anything. I'd also like to understand the number of inquiries that have been made of the four big—how many do you oversee—Deloitte, KPMG—

CHAIR: Senator O'Neill, I might suggest a better course of action. You asked a number of questions intertwined with a number of statements and affirmations. If you've got some questions, why don't you just provide those and that way the committee will get more detailed—

Mr Day: If I might assist, Chair, probably what we could best provide to Senator O'Neil and the committee more broadly is a general briefing on the work of the group, the coverage of the group and the skills of the group, and that, potentially on the next occasion, might allow Senator O'Neil to ask more specific questions.

Senator O'NEILL: Thank you.

Answer

Team experience and structure

ASIC's audit firm inspections are undertaken by members of ASIC's Financial Reporting & Audit team, over 90% of whom are members of Chartered Accountants Australia and New Zealand or CPA Australia.

The Financial Reporting & Audit team comprises 30 staff (27.6 full time equivalents). About 50% of their overall time is devoted to audit inspections. Team members have total average 15 years' audit experience, around half of which is in the ASIC audit related programs.

The Financial Reporting & Audit team also undertakes ASIC's surveillances of financial reports, auditor surveillance matters, reviews, of SMSF auditor conduct and a number of other regulatory activities relating to financial reporting and audit.

In September 2020, ASIC enhanced the senior resources in the Financial Reporting and Audit team. Doug Niven is Chief Accountant, and continues to be responsible for strategy, policy and technical matters relating to financial reporting and audit. This includes ASIC's international work with IFIAR and IOSCO. The Chief Accountant is responsible for decisions on complex audit and accounting issues, such as those arising from audit inspections or financial reporting surveillances.

Thea Eszenyi became Senior Executive Leader for Financial Reporting and Audit and is responsible for the supervision aspects of the Financial Reporting and Audit team's work including the audit firm inspection program, financial reporting surveillances, and SMSF auditor matters.

Audit inspection program

Our [Information sheet 224 ASIC audit inspections](#) outlines the details of our audit firm inspection program. To assist we provide the following high level summary of the key aspects of that information sheet.

Our audit inspections cover the largest six national firms, and other firms that audit the financial reports prepared under the *Corporations Act 2001* (the Act) by listed entities and other public interest entities.

We review key audit areas in the audit working papers for selected audit engagements. For the largest six audit firms we also assess key aspects of audit firm quality control systems over audits of financial reports. This is based on direct reviews of the design and operation of those systems or evidence from audit files.

Following our review of audit files:

- a) we advise the audit firm about the areas where we consider the auditor did not obtain reasonable assurance that the financial report as a whole was free of material misstatement (negative findings)
- b) we ask the firm to identify and commit to remedial actions to address our findings
- c) where we are not satisfied with the audit firm's response to our findings, we will challenge the adequacy of the proposed remedial actions for both individual audits and firm action plans.

The duration of an audit inspection would typically be over a four-week period. Depending on the matters arising from the review the reporting aspect of an inspection can take a several more weeks to complete.

ASIC uses a single risk-based targeting method for selecting financial reports for review in our financial reporting surveillances and for selecting audit files for review in the audit firm inspections.

About 250 financial reports of listed and public interest entities are selected for review each year. Audit files selected for review are generally a subset of the financial reports selected for review.

Approximately 40 to 50 audit files are selected for review each year, the majority of which are from the largest six firms (who audit approximately 93% of ASX listed companies based on market capitalisation) with the balance selected from the approximately 60 other audit firms that audit one or more ASX listed entities.

We generally determine the number of audit files to inspect at the largest six firms based on the market capitalisation of companies audited by each of the largest six firms. For the 12 months to 30 June 2021 we inspected eight audit files at PwC, KPMG and EY (11 prior year), five at Deloitte (seven prior year) and three each at Grant Thornton and BDO (three each prior year). Ten other audit files were reviewed at firms outside the largest six firms (seven prior year). The number of audit files reviewed each year also depends on ASIC's allocation of resources between different priorities.

We target the audits of those financial reports that we consider may have a greater risk of material misstatement. In some cases, audit related considerations may also be taken into account. Our program does not target individual auditors. Concerns about individual auditors may be addressed by a separate surveillance outside the inspection program.

Each file review involves a primary file reviewer and a quality review by a second experienced reviewer who also attends key meetings with the firm to discuss any findings. Larger reviews (such as a financial institution or a top 100 company) may require additional staff members and senior manager oversight. The allocation of audit inspections to team members and quality reviewers is based on their specific areas of expertise, skills and knowledge with less experienced team members assisting under close supervision on these reviews

There is consultation on more complex aspects of the review and associated findings with other relevant experts within ASIC's Financial Reporting & Audit Team, including the Chief Accountant.

All findings from inspections of individual audit firms are discussed with the firm to ensure we have fully understood all relevant facts and have considered all relevant audit work.

Senior ASIC staff, not involved with the particular inspection, assess, the negative finding for consistency with previous findings at the firm and across different firms.

We consult with an independent external review panel on the method of measuring and reporting aggregate findings from our inspections prior to publishing our annual aggregate inspection report and the largest six firm reports. The panel also considers our measurement and reporting methodology and reviews and tests our conclusions reached on a small number of our review findings.

We set out the findings from our inspections in the annual audit inspection report which includes statistics showing the proportion of key audit areas reviewed where we considered the auditor did not obtain reasonable assurance that the financial report as a whole was free of material misstatement. We do this to facilitate understanding of the extent of our findings and the importance of audit firms addressing underlying root causes of those findings.

ASIC's audit inspection report for the 12 months to 30 June 2021 and the inspection reports on the largest six audit firms were published on the ASIC website on 30 November 2021.