

Mr. Bob Charles,
Chairman,
The Joint Committee of Public Accounts and Audit

Dear Mr. Charles,

In response to the invitation to make submissions to your committee, as advertised in the Australian Financial Review dated 12 April, 2002, I offer the following for your consideration:-

1. There will inevitably be a public perception that, where a firm carries out both audit functions and other services to a company, a conflict of interest can exist. This is not to say that such a conflict will actually exist but the public perception will not be easily swayed by argument to the contrary. Viz. justice not only must be done but must be seen to be done.

2. The major purpose of auditing of public company records is to provide a company's shareholders with a report, albeit a snapshot, as to a company's state of affairs.

3. Whilst auditors are "technically" appointed by shareholders it is almost invariably on the recommendation of the directors.

4. Inasmuch as it is, to my knowledge, usual practice, to submit draft audited accounts to the directors for their approval prior to finalising the audit report to shareholders, there can also exist an opportunity for the audit to be influenced by the directors' views, particularly where the auditor provides "other services". Again, this may not be a reality but there is always the real possibility of a public perception along these lines.

Recommendations:-

1. That the possibility of a public perception of conflict of interest be removed by legislation prohibiting the appointed auditor, the firm or company or partnership with which he is associated, providing any services other than audit services to a company.

2. That the term "audit services" be defined so as to exclude any activity not directly associated with the provision of the report to shareholders. E.g. taxation advice, human resources work, management recommendations, IT services etc. would all be excluded.

3. To ensure that the views of the auditor, when differing with those of the directors, are able to be heard by the shareholders without fear of loss of re-appointment of the auditor, legislation should encourage the reporting of the issues involved together with the views of the parties.

4. Firms carrying out an audit should not be permitted to provide income tax advice to the directors (and their associates) of the company.

Effect of recommendations:-

1. Any perception that audit work is performed "on the cheap" in order to obtain more lucrative "other services" work would be eliminated. Thus, audit tenders must be realistic.

2. Any possibility of conflict between the interests of the directors and the shareholders should be minimised.

3. Auditors would be able to present their views, when different to those of the directors, unencumbered by a sense of threat of replacement.

4. Audits may initially cost more but a firm, specialising in audit work or having a specialised audit group, should be able to perform at a higher skilled and efficient level. To this end, shareholders will reap the benefit.

5. I would envisage that current "other service" work is likely to be re-allocated within the industry in such a way that there will be little, if any, overall loss of revenue in this area to the major firms.

In conclusion, my submission is formulated on the basis that there is a perception in the public arena which needs to be eliminated. Accordingly, my suggestions are framed to eliminate that perception.

Sincerely,
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