



# **Senate Select Committee on Superannuation and Financial Services**

## **Main Inquiry Reference (a)**

### **Submission No. 239**

(Supplementary to Submission Nos. 23, 73, 88, 90, 95, 109, 121, 197, 216, 225, 232, 233 & 237)

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20 August 2001

Ms Sue Morton  
Committee Secretary  
Senate Select Committee on Superannuation and Financial Services  
Parliament House  
CANBERRA ACT 2600

Dear Ms Morton

**APRA SUBMISSION TO THE ROUND TABLE HEARING ON AUDIT**

**THURSDAY 23 AUGUST 2001**

Attached is APRA's submission to the Round Table Hearing on Audit on Thursday 23 August 2001.

Yours sincerely

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## APRA SUBMISSION TO THE AUDIT ROUNDTABLE

Thursday 23 August, Committee Room 2S3, Parliament House, Canberra.

### APRA and External Auditors

APRA frequently meets with auditors to discuss their audit of specific APRA-regulated institutions. APRA also undertakes reviews of audit working papers to ascertain the extent and quality of audits undertaken. APRA also coordinates and/or attends many audit liaison meetings held to discuss issues arising during audits of APRA-regulated institutions.

APRA attempts to avoid duplicating the work undertaken by auditors, and relies on the work undertaken by the auditor except where there are concerns that the auditor may not have adequately performed the audit.

A person may be disqualified by APRA from being an approved auditor of superannuation funds if the person has failed to perform their duties and functions adequately. In addition to auditors being disqualified, APRA refers auditors to their professional bodies for further review or action where concerns such as poor performance or lack of independence, have been identified. In most instances, behaviour that warrants disqualification from auditing superannuation funds also warrants referral to a professional body for consideration of the person's performance as an auditor. In some instances these auditors resign from their professional body before a referral can be made. In other instances, where APRA's concerns have been severe but not to the point that disqualification was warranted, referral to a professional body may be the sole sanction applied.

APRA notes that professional bodies have been receptive to APRA (and its predecessors) referring auditors where there have been concerns in terms of adherence to standards. It is noted that the manner in which accounting and auditing services are provided is as relevant as the content of the standards. To this end, APRA (as has its predecessor) has been working with individual auditors and their professional bodies to improve practices where issues have been identified. APRA has assisted in specialist training jointly provided by the ASCPA and the ICAA.

### *Superannuation Industry (Supervision) Act 1993*

The requirements for external auditors of all superannuation funds supervised by APRA are the same. To become an approved auditor, a person must be a registered auditor under Division 2 of Part 9.2 of the Corporations Act, and a member of a prescribed organisation. SIS Schedule 1AAA stipulates that the auditor must specifically be a member of either the Australian Society of Certified Practising Accountants (CPA), the Institute of Chartered Accountants in Australia (ICAA), the National Institute of Accountants (NIA) or the Association of Taxation and Management Accountants (ATMA). Alternatively, an auditor can be a fellow of the National Tax and Accountants Association.

In contrast, SIS only requires an external auditor of Self-Managed Superannuation Funds (supervised by the ATO) to be a member of one of the accounting bodies listed in the SIS Schedule 1AAA (see above).

In addition to the specific SIS Act and Corporations Act requirements, the professional standards of the accounting bodies (eg, ICAA, CPA, NIA, ATMA) require that before their members undertake any work, they must ensure that they have relevant expertise in the area.

In respect of each year of income, the financial statements and accounts of a superannuation entity must be audited by an approved auditor who is required to give to the trustee of the entity a report in the approved form within the prescribed time as outlined in the SIS legislation (Section 113 of the SIS Act).

In addition to the normal audit of the entity's financial position, the approved auditor of a superannuation entity must undertake a mandatory compliance audit of the entity (Sub section 113(3)(b) of the SIS Act). The compliance audit of an entity should reflect the compliance status of the entity, on a wide range of matters under the SIS legislation for the whole of the entity's year of income. Specifically, the auditor forms an opinion on a fund's compliance with specific provisions of SIS.

A person may be disqualified as an approved auditor by APRA if the person has failed to perform their duties and functions adequately or the person is otherwise not a fit and proper person to be an approved auditor (Section 131 of the SIS Act).

Consideration of accounts (contributions, benefits, reconciliations, crediting rate calculations, asset valuations, preservation) forms a significant part of APRA reviews of superannuation funds. Often this would involve understanding accounting and audit practices including viewing audit working papers. Audit engagement letters and management letters (along with trustee responses) would be reviewed. APRA would also seek to understand the internal quality assurance processes of the audit firm.

If an auditor considers that a contravention of the SIS legislation may have occurred, the auditor must inform the trustee in writing of the matter. If the trustee fails to comply with the auditor's request, or the auditor is dissatisfied with the trustee's response, the auditor is required to provide a written report to the Regulator (Section 129 of the SIS Act). APRA has identified only 2 such referrals, despite there having been 1,410 audit qualifications to annual returns (out of a total population of 10,928) for the 1999-2000 year of income.

A similar notification obligation arises if the auditor forms the opinion that the financial position of the superannuation entity may be, or may be about to become unsatisfactory (Section 130 of the SIS Act).

### *Insurance Act 1973*

Section 46 of the *Insurance Act 1973* (Insurance Act) provides that APRA is required to approve the appointment of the auditor of a general insurer. The auditor has a duty under section 47 to audit the accounts of a general insurer and certify whether the accounts appear to be in accordance with the requirements of the Insurance Act.

Under the new general insurance regime, APRA will require general insurers to appoint both an auditor (and in most cases an actuary) who must comply with prudential standards. The routine reporting responsibilities of the auditor are prescribed under paragraph 27 of draft Guidance Note GGN 220.1: Governance. Both APRA and the insurer are required to receive a certificate from the auditor (attached to the annual financial statements submitted by the insurer to APRA) specifying whether, in the auditor's opinion:

- the insurer has complied with the General Insurance Act, Regulations, Standards, authorisation conditions and directions or has given particulars of any matters that do not appear to be in accordance with those requirements;
- the accounting records of the insurer appear to have been properly kept and to explain the transactions and financial position of the insurer or provide particulars of accounting records that appear not to have been so kept and of transactions that appear irregular or have not been accurately or properly recorded;
- the information and explanations provided by the insurer at the request of the auditor is sufficient or that where requests for information and explanation were not met, the particulars of that information;
- the annual financial statements submitted to APRA are consistent with the accounting records of the insurer and appear to truly represent the transactions and financial position of the insurer, and if they fail to do so, particulars have been provided; and
- there are any matters which will, or are likely to, adversely affect the interests of the insurer's policyholders.

In addition to these routine requirements, under the proposed standards the auditor (or valuation actuary) is required to notify APRA if:

- there have been breaches or potential breaches of prudential requirements; and/or
- there is a material risk to policyholders; and
- where a breach or risk to policyholders has not been remedied after due notification to the insurer.

The auditors will also be prescribed "whistle-blowing" responsibilities under the revised Insurance Act. Paragraph 32 of draft Guidance Note GGN 220.1: Governance sets out when an independent expert will be required to provide information to APRA in accordance with this responsibility.

APRA would also like to consider the option of putting in place arrangements with auditors similar to those that exist for banks under the tripartite arrangements. The main focus would be on the accuracy of the quarterly statistical returns. The requirements would need to be outlined in a prudential standard and would be subject to extensive consultation before implementation.

*Life Insurance Act 1995*

Section 83 prescribes that a life insurer must ensure the records of the insurer are audited by the auditor. Section 85 of the *Life Insurance Act 1995* (Life Act) deals with the approval of an auditor by APRA for a life insurer. Section 88 imposes "whistle-blowing" responsibilities on the auditor of a life company.

*Banking Act 1959 and the ADI Prudential Standard*

Section 16B of the Banking Act requires a person who is or has been an auditor of an ADI, authorised non-operating holding company (NOHC) or a subsidiary of these institutions to inform APRA if there are reasonable grounds for believing that the ADI, authorised NOHC or subsidiary of these institutions:

- is insolvent or there is a significant risk to become insolvent;
- has failed to comply with a prudential standard, or a requirement, regulation or direction under the Banking Act, or a condition of the ADI/NOHC authority; or
- an existing or proposed state of affairs may materially prejudice the interests of depositors of the ADI.

This section also provides APRA with the power to request a person who is or has been an auditor of an ADI, authorised NOHC or a subsidiary of these institutions to provide information about the ADI, authorised NOHC or subsidiary if APRA considers that the information will assist it in performing its functions.

Section 16C of the Banking Act also provides for a person who is or has been an auditor of an ADI, authorised NOHC or a subsidiary of these institutions to give information about the ADI, authorised NOHC or subsidiary if the person considers that the information will assist APRA on a voluntary basis if the person considers that the information will assist APRA in performing its functions.

Under paragraph 13 of the ADI Prudential Standard (APS 310 - Audit & Related Arrangements for Prudential Reporting), external auditors of ADIs are required to report annually to APRA on whether:

- the ADI has observed all the prudential standard requirements which APRA has set for the ADI;
- the statistical and financial data provided by the ADI to APRA are reliable;
- the ADI has complied with statutory banking requirements, any conditions on the authority to carry on banking business, any other conditions imposed by APRA in relation to the ADI's operations; and
- there are any matters which, in the auditor's opinion, may have the potential to prejudice materially the interests of depositors of the ADI.

Since 1996 the power has existed to ask external auditors to undertake specific reviews of a particular aspect of a bank's operations or risk management systems.

The cost of these reviews are borne by the banks. Each year APRA has generally asked auditors to undertake a specific review for all banks. To date areas reviewed by external auditors have covered management information systems, business continuity planning, operational risk management, effectiveness of internal audit, outsourcing arrangements, and relationships with other group entities.