

## CHAPTER 5

### THE ROLE OF THE PROFESSIONAL BODIES

5.1 This chapter discusses the part played by the professional bodies for auditors and actuaries, in particular:

- the role of professional bodies for auditors and actuaries in the regulation of superannuation; and
- the qualifications and experience required of auditors under the SIS Act.

#### **The role of professional bodies**

5.2 Professional bodies have an important part to play in ensuring appropriate standards of auditing for superannuation funds. Their means include:

- setting appropriate standards for membership, which in turn qualify auditors as approved auditors under the SIS Act;
- providing education and training to members;
- working with the regulators where appropriate; and
- taking disciplinary action.

5.3 Before opening these issues to discussion, the Chair reminded participants that the purpose of the roundtable was to develop more early warning signals to help prevent fund failure. Referring to the list of 10 key audit issues for superannuation funds identified by Mr Rassi in 1999 (discussed in the Committee's First Report<sup>1</sup>), the Chair asked participants to consider proactive measures to try to lift the standard.<sup>2</sup>

#### *Education and training*

5.4 Representatives of the professional bodies outlined a range of continuing educational programs that were in place for auditors. Mr Malkin from CPA Australia stated:

The profession — certainly CPA Australia and the [ICAA] — is constantly revising the training and education programs for auditors of super funds ... Those types of programs are being continuously updated and strengthened. We are recognising all the types of error messages that Mr Rassi has

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1 Senate Select Committee on Superannuation and Financial Services, *Prudential Supervision and Consumer Protection for Superannuation, Banking and Financial Services: First Report*, 2001, paras 3.15 – 3.17.

2 Committee Hansard, p. 1335.

included in this report, and they are being addressed through the education process.<sup>3</sup>

5.5 Ms Susan Orchard from the ICAA elaborated on the type of education and training provided by the professional bodies:

It includes face-to-face education, communication with members on what is happening in super — which we conduct with our superannuation and financial planning practitioners on a weekly basis — as well as education through magazines and other forums that we have to communicate with members. I think we are seeing an improvement in the audit process. The areas that we have highlighted are highlighted back to trustees and, hopefully, we should then see these issues being resolved by the trustees as they become better educated.<sup>4</sup>

5.6 She noted that many of the problems highlighted by auditors ‘really come out of the education of trustees’. This was an area which the superannuation industry as a whole had been committed to addressing, particularly over the last two years through the efforts of APRA, ASFA and other bodies such as the ICAA.

#### *Working with the regulators*

5.7 Mr Agland from the NIA noted that it was important for the professional bodies to work with the regulators.<sup>5</sup> Mr Malkin stated that the ICAA and CPA Australia had ‘a very strong, very healthy relationship with both the ATO and APRA’, noting that the regulators participated in training courses for members.<sup>6</sup>

5.8 There was agreement amongst participants that the communication between the professional bodies and APRA could nevertheless be improved. APRA convenes regular meetings of a superannuation national audit consultative committee, inviting representatives of each of the professional bodies from which superannuation auditors may be drawn as well as the Auditing and Assurance Standards Board, the Australian Accounting Standards Board, ASIC and the ATO. The Committee was told that there had been occasions where not all the bodies had participated in these meetings, due to a ‘communication breakdown as sometimes occurs when bodies change people who are organising things’.<sup>7</sup> At the last meeting in April 2001, for example, no representative of the professional bodies had attended.<sup>8</sup>

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3 Committee Hansard, p. 1335.

4 Committee Hansard, p. 1335.

5 Committee Hansard, p. 1336.

6 Committee Hansard, p. 1337.

7 Committee Hansard, p. 1338.

8 Committee Hansard, p. 1338.

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*Action against auditors whose performance is inadequate*

5.9 There was discussion of what the regulators and professional bodies did when problems with a particular auditor were identified. Mr Brown said that when APRA identified a fund that was in difficulty, as well as working with the trustees:

... we will review how many super funds the auditor is engaged with in deciding how much effort we put into addressing the shortcomings of that auditor. If the answer is few, it may be that we would call the person in and encourage them to expend their energies in ways other than auditing super funds. That is reasonably effective, because in most instances where that happens the person involved audits very few super funds.<sup>9</sup>

5.10 In response to a question from the Committee about APRA's capability to deal with the matters of concern it identifies, Mr Brown said that in order to fully address every issue that APRA discovered, 'we could expand the resources that we use manifold'.<sup>10</sup>

5.11 ICAA representative Mr Reilly suggested an informal mechanism for referral by the regulator to the professional bodies would be beneficial:

... so that [the regulator] could say, 'There is a member there. The member has had some failings and they are not doing a lot of audit work,' or, 'The failings are there. Can you help the member?' A lot of our work is in fact in the education area. People are fallible; they do make mistakes along the way. They may only be small mistakes and our disciplinary area is seen as hitting people hard, but quite a lot of the time the discipline committee is saying, 'You've got it wrong. What's the answer?' and the member has said, 'Sorry. These are the things that I have put in place to make sure it's right next time around.' It would depend on the severity of the issues. So we are open to working with [APRA] and with the ATO on that basis, as well.<sup>11</sup>

5.12 However, Mr Brown said this informal approach was not possible under the current legislation:

Because there is a formal power in the SIS Act for us to refer and because that can be seen as detrimental to the interests of the auditor, it is not open for us to pick up the telephone and say, 'Hey, we've got a problem with such and such an auditor.' We have to go through a formal process of giving that person natural justice. We have to give them an opportunity to respond to the issues that we have with them and then the referral has to be formal, unless it is that the auditor, of his or her own volition, is prepared to come to the professional bodies and say, 'APRA had these concerns with me and suggested I take on a certain level of training.' But, given both the secrecy

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9 Committee Hansard, p. 1336.

10 Committee Hansard, p. 1336.

11 Committee Hansard, p. 1336.

provisions within the APRA Act and the formal referral provisions within the SI(S) Act, there is not the capacity for us to work at that sort of informal level.<sup>12</sup>

*Other issues: improving trustees' performance*

5.13 Participants also discussed some of the ways in which the performance of trustees could be enhanced, noting that the audit process was designed to identify problems. Mr Rassi commented that there had been improvements in relation to some issues that had been identified in 1999, particularly in relation to the timely finalisation and lodgement of fund accounts which was a matter 'we have been drumming into all our clients'.<sup>13</sup>

5.14 APRA representative Mr Brown said that legislative amendments that changed certain SIS Act offences to strict liability offences from January 2001 had helped in improving the performance of trustees in terms of their record-keeping:

Previously, if a trustee kept the accounts in a shoebox and they were a total shambles, to launch a prosecution it had to be proven that that failure to maintain the records properly was reckless or deliberate. Now it is sufficient to simply prove the fact of failure, although there are statutory defences. We have not yet launched a prosecution under those strict liability provisions, but we have already seen, very strongly, that the change in the legislation has focused trustee attention remarkably. When we go and talk with trustees and we have difficulties with a particular fund, we see that the willingness of the trustees to respond promptly and effectively has been very much enhanced. Even before we have implemented the powers that we have been given, their beneficial effect is being seen.<sup>14</sup>

5.15 Another APRA representative, Mr Venkatramani, said that APRA's power to accept enforceable undertakings from trustees and other associated parties was another valuable tool for the regulator.<sup>15</sup>

*The Committee's view*

5.16 The Committee believes it is essential that the professional bodies and regulators working together to identify common problems in auditing of superannuation funds and develop appropriate training. Effective measures also need to be in place to ensure that 'problem' auditors are identified and appropriate early remedial action is taken, either by way of further training, disciplinary action or exclusion and disqualification where necessary. The Committee encourages the regulators and the professional bodies to keep lines of communication open between

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12 Committee Hansard, pp. 1336-1337.

13 Committee Hansard, p. 1337.

14 Committee Hansard, p. 1338.

15 Committee Hansard, p. 1338.

them. As noted in Chapter 3, the Committee also considers it essential that the professional bodies devote more resources to educating the public about their role.

5.17 The Committee notes APRA's concerns about natural justice in terms of the suggestion that the regulators might provide informal advice to the professional bodies about auditors about whom they may have concern. However, the Committee considers that APRA in conjunction with the professional bodies should consider ways in which this issue might be addressed, including any amendment to the SIS Act that is required.

### **Qualifications and experience of auditors**

5.18 As outlined in Chapter 2, auditors of superannuation funds regulated by APRA are required to be registered company auditors as well as members or fellows of a prescribed professional body. For auditors of ATO-regulated funds, membership or fellowship of a professional body will suffice. The Committee was interested to explore whether the current standards were sufficient and whether the different requirements for the two types of funds were desirable.

5.19 Mr Agland, General Counsel for the NIA, noted that while the SIS Act and regulations did not expressly require auditors to have suitable experience, this was in effect demanded by their membership of professional bodies:

We have set standards as to the qualifications of members at different levels. We have requirements in relation to ethics and in relation to codes of conduct. We have means to investigate members. We also have requirements in relation to continued professional education. The way the legislation sits, it is taking our rules and our regulations and, in effect, applying those. That puts the pressure onto us as the accounting bodies to ensure that those members out there are appropriate to do these types of audits.<sup>16</sup>

5.20 Mr Agland described the NIA's three levels of membership:

- associate membership, for which a two year Advanced Diploma in Business Accounting was required. The NIA would not consider such a person suitable to audit a superannuation fund because of a lack of the necessary qualifications or experience;
- membership, which requires either a degree or graduate certificate in professional accounting from the University of Southern Queensland (a course which includes subjects on business ethics) plus at least three years' experience; and
- a recently created level of membership, called Professional National Accountant. This level requires a university degree or the Bachelor of Financial

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16 Committee Hansard, pp. 1339-1340.

Administration created by the NIA in conjunction with the University of Southern Queensland. A public practice certificate is also necessary, and 'greater requirements as far as their ethics and codes of conduct are concerned'.<sup>17</sup>

5.21 Mr Agland said that the NIA would prefer only those members at its top Professional National Accountant level to do audits of the superannuation funds regulated by APRA, stating:

It is not so much the qualification that [auditors] take at the beginning; almost as important is their experience level. We think they should have the basics they learn in university or under a course, then they should have certain years out in practice, and then after that taken a course that is more specific to superannuation funds.<sup>18</sup>

5.22 Mr Agland said that the NIA's members tended not to deal with the larger superannuation funds, since their expertise was in dealing with the smaller funds.

5.23 The Committee asked whether auditors should be licensed. Mr Agland did not support that suggestion, on the basis that it might exclude many accountants who were sufficiently skilled to audit the small funds:

Licensing creates problems in and of itself, I think. The registered company auditor is a clear example of something that was a great idea but the specifications to become an RCA are such that there are very few registered company auditors out there, which forces them to do a lot of work that people of their experience and their skill probably do not need to undertake. There are other people who could undertake a lot of that work. We would not want to see a licensing arrangement that cut off the majority of accountants who would not be able to undertake small superannuation funds. If you want to say that those sorts of people cannot undertake audits of large funds then that is fine but I think in reality the large funds would go to the big accounting firms anyway.<sup>19</sup>

5.24 In response to questioning from the Committee, Ms East said that the ATO was happy with the current requirements that auditors of small self-managed funds need only be members of specified professional bodies.<sup>20</sup> However, Mr Reilly said he was 'not too sure' that the ICAA or CPA Australia were satisfied with those less strict requirements, noting that the ICAA was concerned about inadequate audits of some of the smaller funds because of the implications for the profession:

We have concerns with some of the anecdotal evidence coming back — prior to the ATO becoming involved in the smaller funds — at the ISC level

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17 Committee Hansard, p. 1340.

18 Committee Hansard, p. 1340.

19 Committee Hansard, p. 1341.

20 Committee Hansard, pp. 1341-1342.

and of course via APRA, that some of the smaller funds are not being audited appropriately. Our quality review program has tended to suggest that that is a fairly minor area for our members, but we are tarred with the same brush. As soon as a regulator says, 'There has been an audit failing,' we automatically say, 'Well, was it us? Or was it them? Or was it some other group along the way?'<sup>21</sup>

5.25 Mr Reilly explained his concerns about having only a requirement for membership of a professional organisation:

... merely saying that if you are a member of a particular organisation you are then able to do an audit places quite a lot of reliance back on that particular individual and that individual's professional organisation to ensure that they actually comply with the rules. So, whilst I am not about to say that chartered accountants, CPA or NIA members are breaching those requirements, I think the fact that at the APRA level you require a registered company auditor to do APRA funds is appropriate, because at least the registered company auditor structure ensures that that person has met a minimum level of competence over a period of time.<sup>22</sup>

5.26 Mr Reilly said, however, that he did not support the way in which the registered company auditor structure currently operated and that he was aware ASIC also did not support it. He referred to a 1997 report by a Working Party of the Ministerial Council for Corporations which had recommended a move away from experience determined on a strict 'hours-based approach' (that is, only satisfying a requirement for a certain number of hours to be completed) to an audit competency approach.<sup>23</sup> Mr Reilly said he believed that the Government had given a commitment to implement that report and that he hoped legislation to give effect to the recommendations would be introduced by the new Government, since he believed the recommendations had bi-partisan support.<sup>24</sup>

5.27 Mr Reilly went on to say:

One of the issues that the working party report highlighted was the fact that, once you got your ticket, you effectively had it for life. Of the 7,000 registered company auditors that were actually on the ASIC register, there might have been only 4,500 that were active auditors. It is becoming increasingly harder for a professional to become a registered company auditor because of the change in the way that the requirements have been administered. So I think that is good.<sup>25</sup>

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21 Committee Hansard, p. 1343.

22 Committee Hansard, p. 1342.

23 Report of a Working Party of the Ministerial Council for Corporations *Review of Requirements for the Registration and Regulation of Company Auditors*, AGPS 1997.

24 Committee Hansard, p. 1342.

25 Committee Hansard, p. 1343.

5.28 Mr Reilly suggested that tighter requirements might be needed for auditors of the small funds regulated by the ATO:

The Institute and CPA Australia are uncomfortable with the fact that there are some other organisations — and I am not necessarily referring to the NIA ... — where mere membership does not give any indication of audit competence. I would argue that mere membership of the Institute or CPA Australia by itself does not necessarily mean you are a competent auditor — further requirements and training are involved.

We would like to think that this committee — once we have an audit competency regime in place — can look at utilising that rather than just mere membership of a professional body in terms of doing the audit of any superannuation fund.<sup>26</sup>

#### *The competency-based approach*

5.29 Mr Reilly explained the ICAA's approach:

... the model that we have worked on is a logbook type structure where you gain experience on particular audits and then work under the direction of a registered company auditor, who is the mentor. The registered company auditor signs off once the particular person has met and demonstrated that degree of competence. It is a much better way than it simply being a matter of hours.<sup>27</sup>

5.30 He went on to explain the disadvantage of the 'hours worked' approach:

The problem with the hours approach is that if you come from a small practice you simply are not going to get the number of hours that you would have from a larger practice, or if you come from a major practice you may spend quite a lot of your time doing other work than audit work. You can spend a lot of hours and still be pretty incompetent. That is not directed at anyone — it is anecdotal evidence. Present company excepted. We think it is a far better approach and it is the approach that the major accounting organisations are using. They are saying that before you are promoted from being an audit senior to an audit supervisor to an audit manager to an audit partner, you have to demonstrate that you have reached appropriate competency levels, otherwise you do not go any further. Competency has certainly been supported over the last 10 years in a whole range of different training areas.<sup>28</sup>

5.31 Mr Shanahan also supported competency standards as 'essential', stating that the industry needed to be 'much more rigorous in auditors of superannuation funds

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26 Committee Hansard, p. 1343.

27 Committee Hansard, p. 1344.

28 Committee Hansard, p. 1344.



meeting the experience qualification'.<sup>29</sup> However, he also considered more was needed by way of a licence 'or a separate chapter of superannuation auditors', stating that the problem:

... is a lack of experience and knowledge of the legislation. The legislation is complex. We keep amending acts. The regulations keep changing. APRA bring out guidance every two years, an addendum in between, and then toss in derivatives as well.

It is complex. You need specialist knowledge. I have no problem saying, 'I would like to see specialist people there.' I do worry if we say, 'Great news to the rest of the world: we now have better superannuation auditors.' ... People will say, 'Well, so what?'<sup>30</sup>

### *Where the problem might lie*

5.32 Mr Shanahan also said that he did not consider the problem lay with the staff who actually carried out the audits, but instead at a more senior level:

... my experience is that I have a great degree of confidence in the staff that do the audits. I believe the people we recruit into the auditing profession from universities with our in-house training do a great job. They find everything that needs to be found. It is in the audit management, the audit supervision and partner clearance level where people make the decision: 'Oh, we have seen that; we can live with it.' I have got a great belief in the ability of our audit staff; I do worry about some of our audit management ...

In audit files I examine in investigatory work, I find that everything that needs to be found is documented in the files. You then have to ask the question: why was it not raised in an audit report or the issue resolved with the client?<sup>31</sup>

### *Taking appropriate action against auditors*

5.33 Mr Shanahan said he was concerned about the current system of regulation of auditors, particularly the time taken for the process:

I believe that ASIC has some of the problems that APRA has. If an audit failure is identified by a regulator you have to follow a due process at law and immediately they bring in lawyers and the whole thing slows down. I do not believe that the self-regulation practised by the professional bodies is as speedy or as efficient as some would have us believe.<sup>32</sup>

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29 Committee Hansard, pp. 1308, 1344.

30 Committee Hansard, p. 1345.

31 Committee Hansard, p. 1345.

32 Committee Hansard, p. 1346.

5.34 In response, ASIC representative Mr Mackintosh noted that while the process was sometimes ‘cumbersome’, principles of natural justice had to be followed.<sup>33</sup>

5.35 Mr Shanahan said he believed the system of self-regulation needed strengthening, citing as another example the available disciplinary remedies:

If people get disciplined by the CALDB [Companies Auditors and Liquidators Disciplinary Board] then they are reported to the Institute or CPA Australia and quite often they say, ‘You’ve been dealt with. We won’t do anything more than that. You can’t have double jeopardy.’<sup>34</sup>

5.36 APRA representative Mr Brown noted in response that APRA had disqualified ‘in the order of 20 auditors over a period of time’.<sup>35</sup>

5.37 The Committee was interested to ascertain the number of auditors who had been disciplined or excluded by the professional bodies. In response to the Committee’s questions on notice, the ICAA advised that four people had been excluded from its membership in the last two years, although none of those cases concerned audit function matters. While the ICAA does not maintain statistics about the source of particular complaints, a review of its disciplinary files for the past three years indicated that APRA had referred three matters to it. The ICAA noted, however, that the discipline of registered company auditors was the primary responsibility of the Companies Auditors and Liquidators Disciplinary Board, since only that Board could revoke registration and thus prevent individuals from acting as company auditors.<sup>36</sup>

5.38 As an example of action that had been taken against auditors, the Committee asked about any disciplinary action taken by the professional bodies in two cases, namely those concerning auditors of Adelaide Steamship and AWA. The ICAA noted that ‘by the time the various legal actions had concluded both auditors had retired and the Institute is not aware that any action was taken by ASIC’.<sup>37</sup>

#### *The Committee’s view*

5.39 The Committee acknowledges that the professional accounting bodies seek to position themselves as leaders in finance, accounting and business advice and that they strive through their endeavors to maintain and enhance their high public standing. The profession acknowledges that its success and public recognition is dependent on the commitment and support of members.

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33 Committee Hansard, p. 1347.

34 Committee Hansard, p. 1346.

35 Committee Hansard, p. 1347.

36 Submission No. 241, p. 1.

37 Submission No. 241, p. 1.

5.40 Recognising the endeavors by the professional bodies to maintain and enhance their public standing, the Committee supports the profession's move towards having auditing competency formally assessed, rather than merely having a requirement that a certain number of hours be completed. The Committee considers that superannuation is a specialist area, that experience in this type of work is essential, and that requiring formal assessment of competency in auditing of superannuation funds should proceed as a matter of urgency.

5.41 The Committee also believes that the current system whereby a higher standard is demanded of those who carry out audits of superannuation funds under APRA's regulation is justified. For the small self-managed superannuation funds regulated by the ATO, where all the members are trustees and thus are responsible for the management of their fund, the Committee believes there is insufficient evidence at this time to impose requirements additional to the membership or fellowship of professional bodies that is currently prescribed. However, in light of the concerns expressed by some of the professional bodies at the roundtable about the adequacy of auditing of some of those small funds, this situation should be monitored.

### **Recommendation 8**

**5.42 The Committee recommends that the current move within the accounting and auditing profession to require the formal assessment of competency in auditing superannuation funds proceed as a matter of some urgency.**

**Senator John Watson  
Committee Chair**

