



## Australian Government

### The Treasury

23 January, 2004

Office of the Secretary  
Public Company Accounting Oversight Board  
1666 K Street, NW  
Washington, DC 20006-2803  
USA

Dear Mr Secretary

#### **RULEMAKING DOCKET MATTER NO. 013**

We appreciate the opportunity to provide a submission in response to the Public Company Accounting Oversight Board's *Proposed Rules Relating to the Oversight of Non-US Public Accounting Firms* (Proposed Rules) released on 10 December 2003.

We support the efforts of the Public Company Accounting Oversight Board (PCAOB) in pursuing the objectives of improving audit quality, ensuring effective oversight of audit firms and helping to restore the public trust in the auditing profession. Australia shares the United States' regulatory objectives in this area.

We understand that, in the interest of minimising administrative burdens and legal conflicts as well as conserving resources, the PCAOB will be actively seeking to rely on the home country's system in situations where it has confidence in that system's integrity. Given Australia's strong regulatory system and the fact that Australia has only a limited number of companies which are SEC registrants (and their debt and equity raisings in the US result in comparatively minor exposure for US investors), we are in favour of an oversight approach by the PCAOB which avoids regulatory overlap with Australia and minimises compliance costs for Australian audit firms that audit SEC registrants. We also agree with the PCAOB's proposal to extend its registration deadline for non-US firms to 19 July 2004.

It should be noted that Australia has been implementing a continuous corporate law economic reform program (the CLERP initiative) since 1997. The aim of this initiative is to ensure that Australia has an effective corporate disclosure framework that incorporates the world's best practice and provides the structures and incentives for a fully informed market.

The following submission outlines how Australian bodies could collaborate with the PCAOB in carrying out its functions under the proposed rules. The submission also provides information about the systems in place in Australia to regulate and oversee accounting and auditing practices, including anticipated changes under the Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Bill 2003 (CLERP 9), which was introduced into Parliament on 4 December 2003, and the role of the Financial Reporting Council (FRC) and the Australian Securities and Investments Commission (ASIC) in the oversight and regulation of the industry.

#### **Australia's regulatory and oversight system**

Australia has a robust, independent and transparent corporate reporting and governance framework. Audits are generally conducted professionally and competently in accordance

with recognised auditing standards, giving full regard to the interests of shareholders, the need for independence, and professional ethical rules. Australia's regulatory system is based on the belief that restoring investor confidence in auditing requires transparent standard setting, effective monitoring and oversight of the financial reporting framework and effective enforcement by the regulators. Each of these aspects will be further strengthened by the CLERP 9 reforms.

#### *CLERP 9 reforms*

The CLERP 9 reforms will significantly strengthen the regulatory requirements applying to company auditors and include measures that:

- move the Australian Auditing and Assurance Standards Board (AuASB) under the authority and oversight of the FRC;
- enhance the financial reporting framework by expanding the powers of the FRC to include monitoring of professional bodies, audit firms and independence policies and procedures;
- improve auditor registration requirements;
- strengthen existing auditor independence requirements through:
  - the introduction of a general standard of auditor independence (based on the corresponding standard in the SEC rules on auditor independence);
  - increased restrictions on employment and financial relationships between auditors and their clients;
  - increased requirements for disclosure of fees for non-audit services;
  - a requirement for audit partner rotation every 5 years;
  - making breaches of the above requirements offences for which ASIC will be able to take appropriate enforcement action; and
- give auditing standards legislative backing.

Generally, CLERP 9 will place liability for contraventions of the law on:

- individual auditors;
- in the case of firms - on each individual partner; and
- in the case of authorised audit companies - on the directors and the company.

#### *Australian Securities and Investment Commission*

ASIC is responsible for surveillance, investigation and enforcement of the Corporations Act, including the statutory responsibilities of auditors and others in relation to financial reporting. ASIC may take action where audits are not undertaken in accordance with the auditing standards.

#### *Financial Reporting Council*

Under CLERP 9, the FRC will oversee the AuASB and have a role in promoting, overseeing and monitoring auditor independence in Australian firms. Ensuring the quality of, and compliance with,

auditor independence standards facilitates both the production of quality audits and the restoration of public trust in the auditing profession. The FRC will not have an enforcement role, as this will remain a matter for ASIC as the securities regulator. However, it is envisaged that the FRC would refer matters of concern to ASIC for investigation, and have a key role in understanding and reporting to the Government on audit firm processes and auditor independence issues more generally.

### **PCAOB's Proposed Rules relating to the Oversight of Non-US Public Accounting Firms**

#### *Registration and information requirement*

While Australian law does not require the registration of audit firms, there is a system of individual auditor registration and provision for deregistration or the imposition of other sanctions where an auditor breaches the law.

We understand that the proposed rules will require individual audit firms to provide the PCAOB with information about the regulatory system in the jurisdiction in which they reside. To this end, the Australian Treasury is willing to provide the PCAOB with relevant material concerning the Australian regulatory system. We suggest that this may be a more efficient means by which to satisfy the PCAOB's information requirement.

#### *Inspection requirement*

As well as responding to the financial reporting issues that are brought to its attention, ASIC conducts extensive reviews of listed entities' financial reports on a routine, not-for-cause basis. ASIC aims to complete about 440 of these reviews in the current year.

ASIC's examination of an entity's financial reports often raises questions about the adequacy of the audit, and in some cases more general issues about the overall level of compliance by an audit firm with its obligations under the current regulatory regime. ASIC pursues these concerns by audit paper review and, where necessary, on-site visits. ASIC investigations of this kind most commonly result in ASIC taking the matter to an independent disciplinary tribunal - the Companies Auditors and Liquidators Disciplinary Board (CALDB). The CALDB was established under the ASIC Act and has a chairman who is a legal practitioner appointed by the Minister. The CALDB has the power to cancel or suspend the registration of an auditor, limit future audit practice, or require other remedial steps. In its last reporting year, ASIC action resulted in disciplinary action against six auditors.

As part of its planning for the new regulatory regime established by the CLERP 9 legislation, ASIC has established a special audit response team. This team is responsible for examining complaints about auditor conduct and investigating individual instances where defects in financial reporting by listed entities are, at least in part, attributable to defects in the audit process.

More significantly, the special purpose team will conduct routine surveillances of auditors to monitor compliance with the enhanced obligations of auditors under CLERP 9. Techniques will include the review of audit papers and regular on-site inspections. ASIC envisages that inspections of larger audit firms (the "Big Four" plus second tier firms) will take place over a two year cycle, with inspections of representative samples of smaller firms done on a risk-scoring basis.

ASIC will examine all material relevant to auditors' compliance with their obligations under Australian law. The initial focus for larger firms is likely to be on compliance with independence requirements, but will extend to all aspects of compliance with legislative obligations. Compliance

with audit standards will be legislatively mandated under the new regime, and this work will therefore encompass all aspects of the audit process.

ASIC's new programs and activities are scheduled to begin on commencement of the new CLERP 9 regime, which is anticipated to commence on 1 July 2004. Some aspects of ASIC's planning for this work are as yet incomplete. However, ASIC is willing to provide further details in order to assist the PCAOB.

#### *Sanctions*

As noted above, while Australian law does not require the registration of audit firms, there is a system of individual auditor registration and provision for deregistration or the imposition of other sanctions where an auditor breaches the law. These sanctions could include:

- the cancellation or suspension of the person's registration as an auditor;
- admonishing or reprimanding the person; and/or
- requiring the person to give an undertaking to engage in, or refrain from engaging in, specified conduct.

#### *Information sharing and scope for cooperative arrangements*

Regarding the issue of sharing confidential information and documents with the PCAOB, we are currently exploring whether any legal or practical problems exist which might impede this process. Information concerning this issue and additional details regarding Australia's regulatory regime could be provided to the PCAOB following the enactment of the CLERP 9 Bill.

We understand that the PCAOB intends to provide a level of assistance that is consistent with the Board's determination regarding the non-US oversight system's level of independence and rigor. In keeping with this, we anticipate that any additional resources or technical expertise required by ASIC to meet the PCAOB's requirements would be provided by the PCAOB.

In summary, we agree that - as generally expressed in the PCAOB's 10 December 2003 release - it is in the interests of the PCAOB and its Australian counterparts, as well as in the public interest, that an efficient and effective cooperative arrangement is developed where reliance is placed on the home country's regulatory system to the maximum extent possible. In this regard, Australia will be taking a close interest in the application of the PCAOB's rules across other jurisdictions, particularly those with similar regulatory regimes to Australia.

We look forward to developing a successful working relationship between the PCAOB and the relevant Australian bodies regarding the oversight of Australian audit firms.

Yours sincerely

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