Joint Accounting Bodies
CPA Australia Ltd, The Institute of Chartered Accountants in Australia & The Institute of Public Accountants

Independence guide

Fourth edition, February 2013

The Joint Accounting Bodies

The major professional accounting bodies in Australia established the Joint Accounting Bodies to speak with a united voice to government bodies, standard setters and regulators on non-competitive matters affecting the profession. The members of the Joint Accounting Bodies are:

CPA Australia is one of the world's largest accounting and finance bodies, representing over 144,000 accounting and business professionals globally.

Our aim is to enhance our members' professional knowledge and support their career development. We do this in many ways, starting with the world-class postgraduate CPA Program, recognised internationally as a benchmark of quality and employability. Thereafter, we deliver a range of continuous learning programs, utilising our international networks to source leading-edge content and presenters.

What sets us apart from other similar bodies is our focus on strategy, leadership and international business. CPA Australia is the global professional accountancy designation for strategic business leaders.

We support our members and the profession internationally by advocating for change at the highest levels and contributing to leading networks worldwide in the finance, accounting and business arenas.

A strategic priority and commitment for CPA Australia is to not only advocate on behalf of members, but also to speak up on economic and political issues in the public interest.

CPA Australia's members are bound by a strict professional code of conduct, including an obligation to undertake continuous professional development to ensure that the highest professional standards are maintained.

Our commitment to excellence, integrity and innovative thinking means that CPAs will remain at the forefront of business and public service now and in generations to come. For further information about CPA Australia visit **www.cpaaustralia.com.au**

The Institute of Chartered Accountants in Australia (the Institute) is the professional body for Chartered Accountants in Australia and members operating throughout the world.

Representing more than 72,000 current and future professionals and business leaders, the Institute has a pivotal role in upholding financial integrity in society. Members strive to uphold the profession's commitment to ethics and quality in everything they do, alongside an unwavering dedication to act in the public interest.

Chartered Accountants hold diverse positions across the business community, as well as in professional services, government, not-for-profit, education and academia. The leadership and business acumen of members underpin the Institute's deep knowledge base in a broad range of policy areas impacting the Australian economy and domestic and international capital markets.

The Institute was established by Royal Charter in 1928 and today has more than 60,000 members and 12,000 talented graduates working and undertaking the Chartered Accountants Program.

The Institute is a founding member of the Global Accounting Alliance (GAA), which is an international coalition of accounting bodies and an 800,000-strong network of professionals and leaders worldwide. For more information about the Institute visit **charteredaccountants.com.au**

The Institute of Public Accountants, established in 1923, provides guidance and insight into long-term future planning for its 22,000 members and students in Australia and more than 50 countries worldwide, as well as quality education and career progression pathways for members and graduates throughout Australia.

IPA members must meet prescribed standards of education, including the IPA Program leading to the degree of Masters of Commerce (Professional Accounting) and experience whilst at the same time displaying the highest ethical and professional standards. The IPA provides expert representation as well as the crucial technical tools and business support members require.

The IPA also provides members with an ongoing program of professional development and a host of social and business networking opportunities and online discussion forums.

IPA members benefit from the organisation's strong alliances and leadership reaching to the international and national business sectors, Australian State and Federal Governments and the wider public and private sectors.

Through these networks the IPA provides 'thought leadership' in addressing issues affecting accounting. As a full member of the International Federation of Accountants (IFAC), the IPA is well positioned in its work with national and international standard setters to ensure members are fully represented and fully informed.

For further information about the IPA visit **www.publicaccountants.org.au**

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Foreword

In today's competitive world trust and confidence are essential to the stability of capital markets. The auditing profession plays a critical role in the orderly functioning of capital markets by performing independent audits. The independence of the auditor is crucial to this process and helps to build the trust of shareholders, regulators and other stakeholders in financial information which has been subject to audit.

In Australia, the independent audit is regulated by legislation, predominantly the Corporations Act (2001), Australian Auditing Standards, and APES 110 Code of Ethics for Professional Accountants (the Code) issued by the Accounting Professional & Ethical Standards Board (APESB).

Produced by the Joint Accounting Bodies, this Independence Guide is intended to assist professional accountants in understanding and applying the auditor independence requirements of the Code.

A key benefit of the guide, which was originally published 13 years ago, is the way in which it provides practical scenarios to guide members in understanding the range of independence obligations they need to comply with under the Code. This fourth edition also includes an expanded section highlighting independence obligations for practitioners auditing self-managed superannuation funds (SMSFs), clarifying potential misconceptions around auditor independence obligations in relation to SMSFs.

I commend the professional accounting bodies for continually providing the necessary resources, such as this guide, to help their members meet professional obligations and maintain high standards of service to clients.

I trust members of the professional accounting bodies who act as auditors find the Independence Guide a useful tool to determine their independence obligations under the Code.

Kate Spargo
Chairman
Accounting Professional & Ethical Standards Board

1. Purpose of the guide

This guide is intended to provide a clear indication of the conceptual approach set out in Sections 290 and 291 of APES 110 *Code of Ethics for Professional Accountants*. It provides practical examples of independence issues encountered by accountants and auditors. The guide is designed for members in public practice addressing independence in the context of assurance engagements. It is not intended to replace APES 110, nor is it intended to be a substitute for any other legal, regulatory or professional standards affecting independence. It is recommended that members become familiar with the Code and other applicable independence standards prior to reviewing any arrangement to ensure independence is maintained.

The examples are illustrative in nature and not intended to, nor can they, include every circumstance that may be applicable when applying the independence standards. The examples are not a substitute for reading and applying the independence standards to the particular circumstances faced by a member. Individual circumstances should be tested against both Section 290 and 291 of the Code, and professional or legal advice obtained if necessary.

1.1 Background

This guide was originally published as an initiative of CPA Australia and the Institute of Chartered Accountants Australia (the Institute) in October 2005 following significant consultations with the Commonwealth Treasury and the Australian Securities and Investments Commission (ASIC), and ongoing member input regarding the application of the Professional Independence Standards. The National Institute of Accountants, now the Institute of Public Accountants (IPA), cooperated with the Institute and CPA Australia to develop and publish an updated guide in June 2008. The 2008 update addressed practical application of the additional requirements in relation to independence arising from the Corporate Law Economic Reform Program Part 9 (CLERP 9).

The CLERP 9 approach recognised the responsibility of the auditor and the directors or audit committee, where applicable, to ensure that the auditor's independence is not impaired.

In the co-regulatory environment, post CLERP 9, the professional bodies established the Accounting Professional and Ethical Standards Board (APESB) to set the code of professional conduct and professional statements by which their members are required to conform, to ensure that standards continue to be robust and transparent, and in the best interests of the public and the profession. The APESB sets ethical and professional standards. It published *The Code of Ethics for Professional Accountants* in July 2006 as APES 110. This was based on the International Federation of Accountants (IFAC) Code of Ethics and contained requirements previously set out in Professional Standard F.1. APES 110 was updated in February 2008 to enact amendments following *The Corporations Legislation Amendment (Simpler Regulatory System) Act 2007* (passed in June 2007).

In December 2010, APES 110 was reissued, with effect from 1 July 2011, to reflect legal and other changes. A summary of current legal, regulatory and professional standards relating to auditor independence is set out in this guide in Appendix 1.

Definition:

Independence standards

In this guide 'independence standards' refers to all applicable legal, regulatory and professional standards affecting independence.

1.2 Key changes

Major changes in this 2013 version of the Independence Guide include:

- Amending the definition of public interest entity to reflect APES 110, issued in December 2011
- Extending independence requirements applicable to audits of listed entities to all public interest entities (including rotation requirements)
- Introducing the concept of a key audit partner
- Introducing guidance to assist in the practical application of the SMSF auditor independence requirements
- Making updates to reflect legislative changes, such as removing the quantitative amount of $5000 that was previously contained in s. 324CH(1) of the Act, but which has been eradicated since the last edition of this guide was issued.

1.3 Acronyms used throughout the guide

The Code and the Act

the Code	APES 110 *Code of Ethics for Professional Accountants* – issued by APESB
Section	Section of the Code (either 290 or 291)
Para	paragraph of the Code
the Act	*Corporations Act 2001*
S	section of the Act

Standards and Regulation

ASA	*Australian Auditing Standard(s)*
ASRE	*Australian Standard(s) on Review Engagements*
ASAE	*Australian Standard(s) on Assurance Engagements*
ASRS	*Australian Standard(s) on Related Services*
APES	*Accounting Professional and Ethical Standard(s)*
ASQC	*Australian Standard on Quality Control for Audit and Review Engagements*

Organisations

APESB	Accounting Professional and Ethical Standards Board	www.apesb.org.au
AUASB	Auditing and Assurance Standards Board	www.auasb.gov.au
ASIC	Australian Securities and Investments Commission	www.asic.gov.au
APRA	Australian Prudential Regulation Authority	www.apra.gov.au

Other

SMSF(s)	Self-managed superannuation fund(s)
EQCR	Engagement quality control reviewer

2. Fundamental principles

Members of the accounting profession have a responsibility to act in the public interest. In doing so, members shall observe and comply with the fundamental principles in the Code:

a) Integrity
b) Objectivity
c) Professional competence and due care
d) Confidentiality
e) Professional behaviour

Members shall be guided by the spirit and not merely the words of the Code

Independence requires an individual member to act with integrity and to exercise objectivity and professional scepticism. Members are obliged to be straightforward and honest in professional and business relationships and not to allow their judgement to be compromised by bias, conflict of interest or the undue influence of others.

Independence comprises both:

- Independence of mind
- Independence in appearance

This means that members must not only be independent in action but they must also be perceived, by an informed third party, to be independent. This is particularly relevant when providing assurance services.

3. Assurance engagements

3.1 Overview

The Code requires members to be independent of assurance clients. An assurance client normally includes the contracted party and its related entities.

Related entity

The definition of a related entity in the Code can be a complex determination involving materiality and other factors. In relation to a company, its 'related entities' could include a holding company, an entity that has a significant influence in the company, its subsidiaries and associates, or any 'sister company' in a group.

The following independence requirements apply in the case of related entities (Paras 290.27 and 291.3):

- For audit and review engagements of a listed entity, the independence requirements of Section 290 apply equally to the related entities of the listed audit client.
- For audit and review engagement of a non-listed entity, the independence requirements of Section 290 apply equally to the related entities over which the audit client has direct or indirect control.
- For all other related entities of a client, the related entities are included when applying the conceptual framework if there is reason to believe a situation involving the related entity is relevant.

For corporate audit clients, there may be other similar terms in the Act that have their own meaning and implications (for example, a 'related body corporate').

In the context of 'assurance engagements', the Code has two sections:

- **Section 290:** Independence requirements for audit and review engagements
- **Section 291:** Independence requirements for all other assurance engagements

It is therefore necessary to understand what an assurance engagement is and how to classify it.

3.2 Classification

An 'assurance engagement' means any engagement in which a member expresses a conclusion that is designed to enhance the degree of confidence of the intended users about the outcome of an evaluation of a subject matter against criteria.

To obtain a full understanding of the objectives and elements of an assurance engagement, refer to the AUASB's *Framework for Assurance Engagements*. The framework is sector neutral and provides guidance on determining whether an engagement involves assurance.

Example of an assurance engagement

An opinion expressed by an auditor on a financial report ('outcome'), which resulted from applying IFRS ('criteria') to a company's financial position, performance and cash flows ('subject matter').

The intended user (such as a shareholder) is separate from the responsible party (the company's directors).

Assurance engagements are undertaken using the standards issued by the AUASB, and as required by governing legislation such as the *Corporations Act 2001*, or the *Superannuation Industry (Supervision) Act 1993* (SIS Act). The following table illustrates which parts of the Code contain the independence requirements that apply to different types of assurance engagements:

All engagements using Australian auditing standards (ASAs), which includes auditing standards that are legally enforceable under the *Corporations Act 2001*, ASA 805 and ASA 810 For example, audits of: • Financial statements/reports • Single financial statements and specific elements, accounts or items of financial statements • Summary financial statements	→	Audit and review engagements – Section 290 applies
All engagements using standards on review engagements (ASREs) 2400, 2405, 2410 and 2415 For example, reviews of: • Financial statements/reports (half-year or full year) • Condensed financial statements or internal management reports • Specific components, elements, accounts or items of a financial report • Other information derived from financial records	→	Audit and review engagements – Section 290 applies
All engagements using standards on assurance engagements (ASAEs) 3000 to 3500 For example, a: • Reasonable or limited assurance engagement to report on greenhouse gas emissions • Performance audit or review to assess the extent to which resources have been economically, effectively or efficiently managed • Service auditor's assurance engagement to report on the description and design of controls	→	Other assurance engagements – Section 291 applies

The crucial tests as to whether an engagement is an assurance engagement are: the three party relationship (assurance practitioner, responsible party and intended user), the subject matter, suitable evaluation criteria, an assurance report, and a process to gather evidence.

The following are not considered to be assurance engagements:

- Agreed-upon procedures engagements (refer ASRS 4400 *Agreed-Upon Procedures Engagements to Report Factual Findings*)
- Compilation engagements (refer APES 315 *Compilation of Financial Information*)
- Preparation of tax returns
- Tax and management consulting work
- Some types of legal and professional services (discussed in paragraph 14 of the *Framework for Assurance Engagements*).

For an understanding of the applicable independence standards affecting different types of entities and assurance engagements, refer to Appendix 2. In this guide, 'independence standards' means all applicable legal, regulatory and professional standards affecting independence.

4. Conceptual framework

4.1 Overview

It is not possible to list every circumstance that can threaten integrity and objectivity. Therefore, the Code contains a conceptual framework through which threats to compliance with fundamental principles are identified and evaluated. Safeguards may be available to reduce the threats to an acceptable level or eliminate it, failing which the engagement should either not be accepted, or the member should withdraw from the engagement.

Conceptual framework

1. Identify threats
2. Evaluate significance of threats
3. Apply safeguards

4.2 Step 1 — Identify threats

The first step is to identify situations that could threaten or appear to threaten a member's independence. The Code contains examples of different circumstances and relationships that can cause threats, categorised as follows:

Threat category	Brief description	Examples in the Code
Self-interest threat	The threat that a financial or other interest will inappropriately influence the member's judgement or behaviour	Para 200.4
Self-review threat	The threat that the results of a previous judgement or service performed by a member will not be appropriately evaluated by the member before it is relied upon in forming a judgement as part of the current service	Para 200.5
Advocacy threat	The threat that a member will promote a client's position to the point that the member's objectivity is compromised	Para 200.6
Familiarity threat	The threat that a member is sympathetic to a client's interest or accepting of their work due to a long or close association with the client	Para 200.7
Intimidation threat	The threat that a member will be deterred from acting objectively because of actual or perceived pressure	Para 200.8

4.3 Step 2 – Evaluate significance of threats

The second step is to evaluate the significance of the threats. Significance is judged by weighing all the specific facts and circumstances, both qualitative and quantitative, and considering whether the threats are at an acceptable level and do not compromise independence.

What is an 'acceptable level'?

A level at which a reasonable and informed third party would likely conclude, weighing all the specific facts and circumstances available, that independence is not compromised.

If multiple threats are identified, they are evaluated in aggregate and safeguards are applied in aggregate, even if the threats are individually insignificant.

4.4 Step 3 – Apply safeguards

If threats are evaluated as significant, the final step is to determine whether appropriate safeguards are available and are capable of being applied to eliminate or reduce the threats to an acceptable level.

The Code classifies safeguards into two broad categories:

Safeguard category	Examples	Further examples in the Code
Those created by the profession, legislation or regulation	The partner rotation requirements in Para 290.151 of the Code and s. 324DA of the Act, together with Regulatory Guide 187 for listed entities.	Para 100.14
Those created in the work environment	A disciplinary mechanism to promote compliance with independence policies and procedures (a firm-wide safeguard), or a requirement to consult with a technical committee for certain pre-defined engagements (an engagement-specific safeguard).	Paras 200.12 and 200.13

A combination of safeguards is often utilised to reduce threats to an acceptable level.

Safeguards may also be created by the systems, procedures or controls of a client. An example of a client safeguard could be a client requiring its audit committee to annually evaluate the independence of the auditor. Other examples can be found in the Code in Paras 200.14 and 200.15. It is not possible to rely solely on safeguards that a client has implemented.

If safeguards are not available or cannot be applied to reduce the significance of any threats to an acceptable level, the only available actions are to eliminate the circumstances creating the threats (if possible), decline the engagement, or end the engagement by withdrawing.

Making an objective assessment

In applying the conceptual framework, members shall always consider what is in the public interest. Stakeholder considerations are more important than those of the client. Evaluating 'independence in appearance' can be particularly difficult.

When finalising a decision, it may be useful to ask these questions:

- Are we being honest and straightforward?
- Are we compromising our judgement?
- Would another member make the same decision?
- Would a third party accept the decision we have made? Do I? Do my colleagues?
- Would we be comfortable discussing the issues with the client or a third party?

4.5 Responsibility

Firms must establish and implement quality control systems and procedures that enable them to identify and manage threats to independence and to ensure compliance with the independence standards (ASQC 1). The type of procedures and individual responsibilities are decided by the firm, depending on its size, operating structure and whether it is part of a network.

The assurance standards require that the engagement partner must form a conclusion on compliance with independence requirements. Independence threats and safeguards need to be evaluated separately for each assurance client and for each engagement period. Engagement teams are entitled to rely on a firm's system of quality control to assist them in managing independence requirements.

Quality control systems

When establishing quality control systems, firms should be aware of the following:

- All partners and staff should be required to have an understanding and working knowledge of the independence requirements
- A 'prevent, detect, report' approach should be encouraged
- Firm-specific policies and procedures must be created to avoid inconsistent interpretations of the independence standards within the firm
- Policies and procedures must be created to deal with instances of non-compliance with the independence requirements, irrespective of whether or not a problem is expected to arise
- The firm's policies must include specific requirements to enable compliance with the *Corporations Act 2001* (for example, by setting specific benchmarks and criteria that make it clear when a responsibility arises to report a contravention of s. 307C (auditor's independence declaration) and when to notify ASIC of a contravention of s. 311 of the Act)
- The firm should devote sufficient ongoing resources to support its quality control system (including, for example, regular training and communication on independence matters)
- The firm must plan and conduct regular testing of its quality control systems

4.6 Documentation

It is crucial that the firm develops policies and procedures specifying the nature and extent of documentation for assurance engagements and for general use within the firm. These policies depend on a variety of factors, such as the complexity of the engagement and the firm's size, structure and assignment of responsibility. The policies are often simply embedded in the firm's audit engagement templates in the form of standard communications, questionnaires, checklists and memoranda. This practice tends to work well to ensure consistent application of the elements of the quality control system at both the firm and engagement level.

Under the Code (Section 290.29), when safeguards are required, documentation on independence shall include:

- Details of issues identified and how they were resolved (such as identification of threats and how safeguards were applied)
- Information about conclusions made and details of relevant discussions that took place

Documentation could also include written confirmation of compliance with policies and procedures on independence from all firm personnel that are required to be independent (refer to Chapter 10).

When a threat requires significant analysis and it is concluded that no safeguards are necessary, documentation could include an explanation of the rationale for the decision.

Overriding requirement for documentation

Prepare documentation that can be understood by an experienced auditor, having no previous connection to the engagement.

'If it's not documented, it's not done.'

4.7 'Small firms' and 'small clients'

Some members of the accounting profession may consider certain types of clients, such as a self-managed superannuation fund (addressed in more detail in Chapter 9) or a small proprietary company, to be a 'small client' where the independence requirements do not necessarily apply. On the contrary, the independence standards apply equally to all assurance engagements, whether large or small.

The size of the client has a direct impact on the type and significance of identified threats. For example, close relationships with a client are often more prevalent between small clients and small accounting practices. This can make it harder to reduce the independence threats to an acceptable level.

In addition, small firms often find it difficult to apply some of the safeguards that would ordinarily be available to a larger firm. For example, it may not be possible for a small firm to segregate the teams that provide assurance and non-assurance services for a client.

Members in a practice, whether large or small, must be vigilant in their approach to independence and apply the independence requirements with rigour to all assurance clients.

4.8 Case study – Application of the conceptual framework

Scenario – An auditor in a small regional centre trades with an audit client because there are no other suitable suppliers available. The terms are the same as are available to all other customers. The outstanding account balance fluctuates between $ 5000 and $ 7000.

Step 1: Identify threats

Self-interest threat:

- The auditor may be reliant on the supplier; this could affect the auditor's behaviour.

Familiarity threat (if the facts support it):

- Members of the audit team may have a long association with the supplier or officers and employees of the supplier.

Step 2: Evaluate significance

Significance is increased by the fact that this is an audit engagement (Section 290 applies).

Factors that could further increase the significance of the threats:

- If the entity is a public interest entity (see Chapter 5)
- There are no alternative suppliers available to the auditor ('qualitative factor').

Factors that may mitigate the significance of the threats:

- The balance does not appear to be substantial ('quantitative factor')
- The terms are at arm's length ('qualitative factor').

Step 3: Apply safeguards

Legislative safeguards:

S. 324CH(1) item #15 of the *Corporations Act 2001* prohibits a firm from owing an amount to the client, unless subsection (5A) applies where goods or services and the related debt arise on normal terms and conditions.

Professional and work-environment safeguards:

- The threats associated with these circumstances would generally be at an acceptable level if the transaction is in the normal course of business and at arm's length (Para 290.126).
- If there are multiple threats or the client is a public interest entity, the significance of the threats would be higher and would require additional safeguards (individually or in combination). For example:
  - (i) A control that no member of the audit team is involved in ordering, taking delivery or paying for goods from the supplier
  - (ii) Rotating senior members of the audit team to reduce the familiarity threat or appointing an engagement quality control reviewer
  - (iii) Setting a limit on the monthly purchases allowed from the supplier.

5. Public interest entities

5.1 Overview

The independence requirements for public interest entities are more extensive than for other audit and review clients, thereby recognising that the extent of public interest in an entity has a direct impact on the significance of identified threats. Appendix 2 sets out requirements by entity classification.

The new term 'public interest entity' introduced in Section 290 has the effect of extending the previous independence requirements that applied to listed entities to a larger group of listed and unlisted entities.

5.2 Effective date

The new definition of a public interest entity was effective from 1 January 2013. The Section 290 provisions are applicable to all audit and review engagements for public interest entities commencing on or after this date. Some transitional provisions apply to areas such as partner rotation (refer Chapter 8).

5.3 Definition

Public interest entities are:

- All listed entities; or
- Any entity (a) defined by regulation or legislation as a public interest entity; or (b) for which the audit is required by regulation or legislation to be conducted in compliance with the same independence requirements that apply to the audit of listed entities. Such regulation may be promulgated by any relevant regulator, including an audit regulator.

Section 290.25

5.4 Responsibility

Firms must establish systems and procedures to determine whether any audit and review clients, or categories of such clients, meet the definition of a public interest entity because they have a large number and wide range of stakeholders. This process will take into consideration the nature of the entity's business, its size and the number of employees.

The timing and individual responsibilities for classifying clients is left to the firm to decide. A firm should regularly evaluate the decisions it has reached regarding its audit and review clients, taking into account any changing circumstances.

Large number and wide range of stakeholders

The following entities are likely to be classified as public interest entities as they tend to have a large number and wide range of stakeholders:

- Authorised/registered deposit-taking institutions, insurers, life insurance companies and non-operating holding companies regulated by APRA under the Banking Act, the Insurance Act or the Life Insurance Act
- Disclosing entities (s. 111AC of the Corporations Act 2001)
- Registrable superannuation entity licensees and the like under their trusteeship that have five or more members, regulated by APRA under the Superannuation Industry (Supervision) Act
- Other issuers of debt and equity instruments to the public.

Section 290.26

6. Networks

6.1 Overview

For audit and review engagements, the independence requirements extend to network firms. In other words, firms that belong to a network are independent of the audit and review clients of other firms in the network.

For other assurance engagements, any threats that a firm has reason to believe are created by a network firm's interests and relationships will be evaluated.

Sections 290.13 to 290.24 of the Code set out explanations in relation to networks.

6.2 Definitions

Whether an association of firms is a network requires judgement that takes into consideration all of the specific facts and circumstances, and whether a reasonable and informed third party would likely conclude that a network exists.

Definitions

The Code defines the following:

Network firm means a firm or entity that belongs to a network.

Firm means:

a) A sole practitioner, partnership, corporation or other entity of professional accountants;

b) An entity that controls such parties, through ownership, management or other means;

c) An entity controlled by such parties, through ownership, management or other means; or

d) An Auditor-General's office or department

Network means a larger structure:

- That is aimed at cooperation; and
- That is clearly aimed at profit or cost sharing or shares common ownership, control or management, common quality control policies and procedures, common business strategy, the use of a common brand name, or a significant part of professional resources.

6.3 Responsibility

Firms and assurance teams must follow procedures to identify, evaluate and address threats to independence arising through network firms. Compliance with these requirements is dependent on whether the whole network coordinates the design, and consistently applies procedures to identify and manage threats to all the audit and review clients within the network.

Which individuals of a network firm must be independent?

- Any individual employed or engaged by a network firm who performs procedures on an assurance engagement, and
- For audit and review engagements, all those within a network firm who can directly influence the outcome of the engagement.

To assist in assessing independence in relation to network firms:

- Network-wide independence policies and procedures could be developed by following the same principles that are used to design a firm's system of quality control. These policies and procedures are then incorporated consistently into the quality control systems of each firm within the network. Regular communication between the firms within the network and ongoing testing of the system is paramount.
- Responsibility could be assigned for the maintenance of a database which lists all clients from whom independence is required, including relevant related entities (see Chapter 3). If used, the database should be easily accessible by all partners and staff within the firm or network and regularly updated.

6.4 Examples

The examples below explore several common scenarios and whether they may involve a network. It is assumed that there are no unmentioned facts which would be relevant.

Facts	Analysis	Conclusion
A is an association of firms formed to provide global services to clients. Each firm is a separate and distinct legal entity. The firms within the association share common quality control policies and procedures. These policies and procedures were designed by A and have been implemented across the association and are monitored across the association. There is annual communication across the association of the scope, extent and results of the monitoring process. Under the association agreement the monitoring of each firm is performed by a group of people from a central location. The monitoring group has the authority to make specific recommendations for action. The conditions of membership require firms to take the recommended action.	**A** is a larger structure aimed at cooperation. The larger structure shares common quality control policies and procedures. Refer Para 290.18.	**A** is a network.
B is an association of firms, operating in 120 different countries, established to provide global services to clients. Each firm is a separate and distinct legal entity. All of the firms are listed in the global directory of B. When performing assurance engagements, all firms use a common audit methodology which was developed by B. Each firm implements its own system of quality control policies and procedures and there is no shared monitoring across the association. All firms mention that they are a member of B association in marketing and promotional material. Eighty firms use the name when signing assurance reports. There are numerous common clients between these 80 firms. The 40 other firms use a local name. There are no common clients between these 40 firms.	**B** is a larger structure which is aimed at cooperation. The 80 firms within the larger structure that use the name of B when signing assurance reports are a network. The other 40 firms, that use a local name when signing assurance reports, are not part of the network. These 40 firms should, however, carefully consider how their promotional material describes their membership in B to avoid the perception that they belong to a network. Refer Paras 290.20, 290.21 and 290.24.	**B** is a network comprised of the 80 firms that use the B name in the signing of assurance reports. The other 40 firms are not part of the network.
C is an international association of firms formed to provide global services to clients. Each firm is a separate and distinct legal entity. Under the profit sharing arrangement, 30 per cent of the profit of each firm is pooled and redistributed to individual firms based on a pre-defined formula.	**C** is a larger structure which is aimed at cooperation. The larger structure is clearly aimed at profit sharing. Refer Para 290.16.	**C** is a network.

Facts	Analysis	Conclusion
D is an association of firms in one country. Each firm is a separate and distinct legal entity. The firms use a common audit methodology and share a common technical department. Under the association agreement, all financial statements must be reviewed by the technical department before the audit report is issued. The advice from the technical department, either on review of the statements or through consultation during the audit, must be followed by the audit partner.	**D** is a larger structure aimed at cooperation. The use of a common audit methodology is not sufficient to conclude that the larger structure shares significant professional resources but there is also sharing of a technical department and the advice from this department is mandatory. This fact, coupled with the requirements for the technical department review of financial statements before release of the audit opinion, would indicate that the larger structure does share significant professional resources. Refer Para 290.24.	**D** is a network.
E is an association of firms in one region. Each firm is a separate and distinct legal entity. A condition of membership of the association is that each firm will ensure its system of quality control for assurance and other related services engagements comply with APES 320 and ASQC 1.	**E** is a larger structure aimed at cooperation but does not share common quality control policies and procedures. The agreement to ensure firms' system of quality control complies with APES 320 and ASQC1 is not the same as sharing common quality control policies and procedures. Refer Para 290.18.	**E** is not a network.
F is an association of firms in one country formed to exchange ideas, information and expertise with the goal of improving the quality and profitability of the firms within the association. Each firm is a separate and distinct legal entity. The association conducts a number of educational programs each year covering matters such as changes in accounting standards. The association also distributes a monthly newsletter on matters of interest. All firms within the association are listed in a members' directory. Member firms use the directory to locate other members for matters such as referral of work or for identifying another firm with whom to partner for a specific piece of work. Many firms within the association indicate on their stationery and promotional materials that they are a member of F association. None of the firms use the F name in signing of assurance reports.	**F** is a larger structure which is aimed at cooperation but it is clearly not aimed at profit or cost sharing and does not share common ownership, control or management, common quality control policies and procedures, a common business strategy, use of a common brand name or a significant part of professional resources. The reference by some firms to the membership of F association does not in itself create a network firm relationship. Such firms should, however, be careful how they describe the relationship to avoid the perception that the association is a network. Refer Paras 290.14, 290.24 and 290.21.	**F** is not a network.
G is an association of 10 firms in one country formed to share expertise to develop audit manuals to comply with new auditing standards. Each firm pays one-tenth of the cost of a small group of experts who are responsible for developing the audit manuals.	**G** is a larger structure which is aimed at cooperation but it is not clearly aimed at profit or cost sharing and does not share common ownership, control or management, common quality control policies and procedures, a common business strategy, use of a common brand name or a significant part of professional resources. The sharing of the costs associated with the development of the audit manuals does not in itself create a network relationship. Refer Paras 290.16 and 290.24.	**G** is not a network.

7. Examples of independence issues

7.1 Overview

The examples that follow are intended to provide guidance on common independence issues that arise in practice. The conceptual framework in Sections 290 and 291 is applied in dealing with each scenario and it is assumed that there are no other unmentioned facts that could be relevant.

The factors that impact the significance of a threat and the safeguards proposed are only examples. Many other factors or actions could apply in any of the given situations. Furthermore, members must apply the specific work-environment safeguards that may be prescribed by a firm or network firm through its system of quality control.

In all situations, members must be mindful of what is in the public interest and, in particular, whether a situation could pass the 'independence in appearance' test. Members should seek advice where necessary.

7.2 Effect of classification as a public interest entity

The provisions of Section 290 that are applicable because of the new definition of a public interest entity were effective from 1 January 2013.

The Code contains a transitional provision for any non-assurance service for an audit client that was allowed by the previous Code, but which is now prohibited or restricted as a consequence of the client being classified as a public interest entity. The auditor may continue to provide such services only if they were contracted for and commenced prior to 1 July 2012, and are completed before 1 January 2013.

7.3 Examples

7.3.1 'The books' are prepared by the auditor

The general principles to apply are:

- For public interest entities, the auditor shall not provide accounting and bookkeeping services or prepare the financial statements of the client, even in emergency situations (Para 290.172).
- For entities that are not public interest entities, the auditor can provide services related to the preparation of accounting records and financial statements that are routine and mechanical in nature and provided the self-review threat is reduced to an acceptable level (Para 290.171).

Scenario – The accounting records (including the trial balance) are prepared by the client. The client has accepted responsibility for preparing the accounting records. The auditor prepares financial statements from the trial balance.

Identify threats	Self-review threat
Evaluate significance	Significance is increased by the fact that this is an audit engagement (Section 290), but mitigated by the fact that the client has taken responsibility for preparing the accounting records. Significance will also depend on: • Whether the entity is a public interest entity • The degree to which the preparation of the financial statements is a routine/mechanical task
Apply safeguards	If the audit client is a public interest entity, the significance of the threat would be too great due to the perceived threat to objectivity and integrity that cannot be overcome. The engagement is terminated or declined (Section 290.172). If the audit client is not a public interest entity, and the services are routine and mechanical, the threat could possibly be reduced to an acceptable level by having a qualified person, who is not a member of the audit team, take responsibility for preparing the financial statements and the client acknowledging their responsibility for the financial statements.

Scenario – The accounting records (including the trial balance) are prepared by the client. The client has accepted responsibility for preparing the accounting records. The auditor prepares financial statements from the trial balance and proposes adjusting journal entries.

Identify threats	Self-review threat
Evaluate significance	Significance is increased by the fact that this is an audit engagement (Section 290) and the auditor has proposed adjusting journal entries, but mitigated by the fact that the client has taken responsibility for preparing the accounting records. Significance will also depend on: • Whether the entity is a public interest entity • The degree to which management is conversant with the changes being proposed by the auditor, while still being able to take responsibility for the final financial statements • The degree to which the preparation of the financial statements is a routine/mechanical task
Apply safeguards	If the audit client is a public interest entity, the significance of the threat would be too great due to the perceived threat to objectivity and integrity that cannot be overcome. The engagement is terminated or declined (Section 290.172). If the audit client is not a public interest entity, it may be possible to reduce the threats to an acceptable level by: • Having the client evaluate the proposed adjustments and accept responsibility for them (Paras 290.166 and 290.169) • Having a qualified person, who is not a member of the audit team, take responsibility for performing the non-audit services and obtaining the client's acknowledgement of responsibility for the financial statements • Establishing procedures within the firm that prohibit the person who provides the non-audit services from making any management decisions on behalf of the client

Scenario – A small client provides original documents and an incomplete trial balance to the auditor. The client is not a public interest entity. The auditor prepares the general ledger, journal entries and financial statements. Consider this example in the following situations:

- **The auditor is a sole practitioner who employs qualified senior managers**
- **The auditor is a firm with more than one partner**

Identify threats	Self-review threat
Evaluate significance	Significance is increased by the fact that this is an audit engagement (Section 290) and the auditor is recording transactions, determining account classification and originating journal entries. Significance will also depend on: • Whether the client was given an opportunity to make an objective and transparent analysis of any decisions made by the auditor before they were recorded (Para 290.166). • The degree to which management is conversant with the decisions made by the auditor and whether they can honestly take responsibility of the accounting records and the financial statements. • The degree to which the preparation of the accounting records and financial statements is a routine/ mechanical task (such as how much subjectivity or judgement was involved).
Apply safeguards	a) If the auditor is a sole practitioner, it will be impossible to reduce the significance of the threats to an acceptable level because there is no opportunity within the practice to segregate ultimate responsibility for the audit engagement from the non-assurance services (even if a qualified senior manager who is not on the audit performs the non-assurance services). The engagement is terminated or declined. b) If the auditor is a firm, it may be possible to reduce the threats to an acceptable level (depending on significance) by: • Having the client evaluate the account classifications and proposed adjustments and accept responsibility for them (Paras 290.166, 290.169 and 290.171). • Having a qualified person, who is not a member of the audit team, take responsibility for performing the non-audit services and obtaining the client's acknowledgement of responsibility for the financial statements. • Establishing procedures within the firm that prohibit the person who provides the non-audit services from making any management decisions on behalf of the client. • Segregating ultimate responsibility for the audit engagement from that of the non-audit services.

Scenario – A client is not a trading entity and has very few transactions. The client expects the auditor to record the transactions in the books prior to preparing and auditing the financial statements. Each transaction and balance is supported by third party documentation. The auditor does not recalculate figures or make any judgements on how to classify amounts in the trial balance. There are no adjusting entries.

Identify threats	Self-review threats
Evaluate significance	Significance is increased by the fact that this is an audit engagement (Section 290), but mitigated by the fact that the auditor's activities are routine or mechanical and require very little judgement to be exercised. Significance will also depend on: • Whether the entity is a public interest entity • The degree to which management is conversant with accounting practices and principles and is able to take responsibility for the accounting records and the financial statements
Apply safeguards	If the audit client is a public interest entity, the significance of the threat would be too great due to the perceived threat to objectivity and integrity that cannot be overcome. The engagement is terminated or declined (Section 290.172). If the client is not a public interest entity, it may be possible to reduce the threat to an acceptable level by: • Obtaining the client's acknowledgment of responsibility for the accounting records and financial statements • Implementing policies and procedures to prohibit the person who provides the services from making any managerial decisions on behalf of the client Note: As the number of transactions increase, the significance of the threat will grow as judgements will increasingly need to be made and amounts will no longer simply agree to third party documents. In that situation, additional safeguards must be applied (for example, by having an independent accountant perform the accounting services) or the engagement is terminated.

7.3.2 Services previously allowed for a public interest entity

Scenario – The auditor of a small listed company has been engaged to perform emergency accounting services for the company.

The Code prohibits the auditor from providing accounting and bookkeeping services for public interest entities, even in emergency situations.

Note: The previous Code (issued in February 2008) allowed emergency accounting and bookkeeping services for a listed entity. The Code contains a transitional provision for any non-assurance service for an audit client that was allowed by the previous Code, but which is now prohibited or restricted. The auditor may continue to provide such services only if they were contracted for and commenced prior to 1 July 2012, and are completed before 1 January 2013.

If the emergency situation was contracted after 1 July 2012, it is a violation of the Code even if the services are completed before 1 January 2013.

7.3.3 Accounting advice

Scenario – The auditor responds to questions by the audit client on the application of accounting standards and the methods to be used to value the assets and liabilities in the financial statements.

Identify threats	Self-review threat
Evaluate significance	Significance is increased by the fact that this is an audit engagement (Section 290) Significance will also depend on: • Whether the entity is a public interest entity • The degree to which management is conversant with the application of accounting standards and valuation methods
Apply safeguards	Para 290.169 recognises the need for dialogue between the auditor and the client on these types of matters. However, answering questions can quickly escalate from a simple dialogue into an act of giving advice and possibly making decisions for the client. Safeguards should be applied to prevent the auditor from assuming management responsibility when providing advice (Para 290.170). Safeguards could include (Para 290.166): • Requiring the audit team to defer any technical questions to a specialist within the firm • Presenting written alternatives to the client in answer to their questions, thus allowing the client to make objective and transparent decisions • Evaluating the ultimate decision of the client, ensuring the reasons for their decisions are self-determined • Obtaining acknowledgement of responsibility from the client for any actions or decisions made

7.3.4 Director or officer

Scenario – A partner is asked to audit a company or trust where a fellow partner is a director/trustee.

Identify threats	Self-review, self-interest and (possibly) intimidation and familiarity threats
Evaluate significance and apply safeguards	Para 290.146 considers the threats in this situation to be so significant that no safeguards can reduce the threats to an acceptable level. The engagement is not accepted. In the case of a corporate audit client, this type of relationship is also prohibited by s. 324CH(1) item #1 of the Act.

7.3.5 Accounts with financial institutions

Scenario – A member of the team conducting the audit of a local bank has an account with the bank.

Identify threats	Self-interest threat
Evaluate significance	Significance will depend on: • The significance or materiality of the account in relation to the team member's affairs • The terms and conditions of the account Significance is increased by the fact that this is an audit engagement (Section 290) and most likely a public interest entity.
Apply safeguards	Paras 290.123 and 290.120 allow team members to have deposit and loan accounts with banks provided they are under normal commercial terms (in the case of deposit accounts) and in terms of normal lending procedures, terms and conditions (in the case of loans). The Act allows similar safeguards for 'basic deposit products' and loans in Section 324CH(1) item #15 and #16 and Section 324CH(5) to (6A).

Scenario – The audit manager on the team undertaking the audit of a bank has a mortgage with the bank. He wishes to draw down additional funds.

The considerations would be similar to the previous example. The Act would allow the original mortgage under s. 324CH(5) 'Housing loan exception' and the drawing down under Section 324CH(5B) 'Ordinary commercial exception'.

At a minimum, the audit partner should be informed. The firm's quality control procedures may require the audit manager to also disclose the matter to the firm.

Scenario – A partner in a firm has a housing loan with a bank which is an audit client. The partner is not involved in the audit and does not provide any other professional services to the bank. The partner wishes to extend the original loan in order to undertake renovations to his home.

The considerations would be similar to the previous examples. The Act would allow the draw down under s. 324CH(5B) 'Ordinary commercial exception'. The firm's quality control procedures may require the partner to disclose the matter to the firm.

Scenario – A partner at an audit firm has an interest in a body corporate which is considering taking out a loan with a bank. The bank is an audit client of the audit firm. The partner does not have any influence on the management of the body corporate or their decision to obtain a loan from the bank. The partner is not involved in the audit and does not provide any other professional services to the bank.

Identify threats	Para 290.115 requires members of the audit team to determine whether a known financial interest (such as this one) creates a self-interest threat. The nature of the relationship between the partner and the audit team and the firm's operational structure could be factors in this assessment. The firm's quality control procedures may require the partner to disclose the matter to the firm. The firm will also need to consider whether the audit partner should be informed.
Evaluate significance	If a threat exists, significance is evaluated. Significance could be increased by the fact that this is an audit engagement (Section 290) and, most likely, the bank is a public interest entity. The significance is reduced by the degree of separation of the partner from the audit team and the bank, and because the partner has no influence over the management of the body corporate or its decision making.
Apply safeguards	If considered necessary, the firm could institute procedures to ensure the partner does not become a member of the audit team. The Act prohibits an entity which a member of the firm controls or a body corporate in which a member has a substantial holding from owing an amount to an audited body. This requirement is set aside under the 'Ordinary commercial loan exception' if the loan is made in the ordinary course of business on normal terms and conditions in Section 324CH(5B).

Scenario – A partner of an audit firm recently purchased a number of household goods. He accepted the store's offer to pay for the goods in 12 months. The store uses a finance company for the transaction and the partner ultimately enters into an interest-free loan (on normal terms and conditions) with the finance company. The finance company is an audit client of the firm.

Identify threats	Possible self-interest threat
Evaluate significance	Significance will depend on (for example): • The nature of the relationship between the partner and the audit team • The firm's operational structure
Apply safeguards	The fact that the arrangement is made in the ordinary course of business on normal terms and conditions may be sufficient to reduce any threat to an acceptable level. In the Act, s. 324CH(1) item #15 prohibits a member of an audit firm from owing an amount to a corporate audit client, except if the 'Ordinary commercial loan exception' in s. 324CH(5B) applies.

7.3.6 Loyalty scheme

Scenario – The audit manager for an audit client joins the client's loyalty program. Points are accrued each time he purchases goods at the client's store. After 10 points, he is entitled to redeem those points for various rewards.

Identify threats	Self-interest threat
Evaluate significance	Significance may depend on: • Whether membership of the loyalty program is restricted to certain individuals, or if membership is available to the public • Whether the points can be redeemed for cash • Whether the rewards can be used as a 'discount' against future purchases
Apply safeguards	The fact that the arrangement is made in the ordinary course of business on normal terms and conditions may be sufficient to reduce any threat to an acceptable level. In the Act, s. 324CH(1) item #16 prohibits a corporate audit client from owing an amount under a loan to a professional member of the audit team. The Act does not define the word 'loan'. It is reasonable to interpret 'loan' as involving moneys owing, owed or payable. Loans usually involve a promise by one person (lender) to pay a sum or sums of money to another (borrower) in consideration of the borrower agreeing to repay that sum of money on demand or at a fixed future date or dates. Under the terms of most retail, frequent flyer or loyalty schemes, no moneys are usually owed or payable. If the auditor is unsure, they should enquire further. A prudent safeguard would be for the audit manager not to have any responsibility for conducting or reviewing the audit work over the loyalty program.

7.3.7 Insurance claim

Scenario – The audit manager on the audit of an insurance company has motor vehicle insurance with the company and was recently involved in a traffic accident. He has instituted an insurance claim. He is waiting for the claim to be processed. The audit manager believes the company is holding back on the claim.

The audit manager should disclose the situation in accordance with the firm's quality control procedures which, at a minimum, would require that he informs an appropriately senior partner of the firm about the situation.

Identify threats	Self-interest threat
Evaluate significance	Significance will depend on: • The size of the claim and how significant or material it is to the audit manager • The reasons for the delay (both actual and perceived) Significance could be increased by the fact that this is an audit engagement (Section 290) and the insurance company is a public interest entity.
Apply safeguards	There is no specific requirement in s. 324CH(1) of the Act relating to insurance arrangements. However, the audit partner is obliged to consider and avoid a conflict of interest situation whereby a member of the audit team is not capable of exercising objective and impartial judgement (refer to Section 220 of the Code and the 'General requirements' in s. 324CB and s. 324CD of the Act). The audit partner will need to decide whether a reasonable person, with full knowledge of all relevant facts and circumstances, would conclude that the audit manager is not capable of exercising objective and impartial judgement in relation to the conduct of the audit. It may require safeguards to be implemented, or the audit manager may have to be removed from the audit.

7.3.8 Ten hour 'maximum hours test'

Scenario – A partner in the tax division of a firm has been asked to assist an audit client with a complex tax issue. The engagement is expected to require more than 10 hours. The partner's wife works for the audit client and receives share options as part of a staff bonus scheme. She is not an officer of the client nor in an 'audit critical' role. The bonus scheme restricts the ability to exercise the options until certain events occur. One such requirement is a minimum service requirement. The couple have always sold shares arising from the bonus scheme as soon as control over the options has vested.

The tax partner should disclose the situation in accordance with the firm's quality control procedures which, at a minimum, would ensure the audit partner is informed.

Identify threats	Self-interest and advocacy threats
Evaluate significance	Significance will depend on: • Whether the client is a public interest entity • The nature of the services (for example, tax advisory or dispute resolution) and the complexity of the matter (such as the degree of judgement involved) • The level of tax expertise at the client and the degree of management involvement in the matter • The extent to which the tax services to be provided will have an impact on the financial statements to be audited • Whether the tax service relates to the options scheme
Apply safeguards	For a corporate audit client the tax partner is prohibited from becoming a 'non-audit service provider' to the audit client (s. 324CH(1) item #10) because of the existence of the bonus scheme and unvested options. The prohibition arises when a partner provides more than 10 hours of non-audit service (the 'maximum hours test'). The provisions of Section 290 are largely irrelevant because of this prohibition in the Act. Threats and safeguards must still be considered if the work is less than 10 hours.

7.3.9 Tax services

Scenario – A firm undertakes tax services for a non-listed audit client.

Firstly, the auditor must determine what is meant by tax services and then apply the conceptual framework. Two scenarios have been addressed here:

(a) The auditor prepares the tax return for the client. The tax issues are not complicated for this client and very little judgement is required.

Identify threats	Self-interest threats
Evaluate significance	Significance may be increased if the client is a public interest entity. Significance may be mitigated, for example, by the fact that the tax issues are not complicated and very little judgement is required.
Apply safeguards	Generally, the preparation of tax returns can be performed, provided the client takes responsibility for the return, including any significant judgements made (Para 290.183). This rule exists on the assumption that the tax return preparation is based on historical information and principally involves analysis and presentation of such information under existing law and precedents. Furthermore, it assumes the tax returns are subject to whatever review or approval process the tax office deems appropriate. The use of separate engagement teams may provide an appropriate safeguard.

(b) The auditor prepares the current and deferred tax liability calculation for the purpose of preparing accounting entries that will be audited by the firm. The person who prepares the computation has done so for over 10 years. The amounts are material to the financial statements.

Identify threats	Self-review and familiarity threats
Evaluate significance	Significance is increased by the fact that this is an audit engagement (Section 290), the amounts are material to the financial statements and because of the long association of the person who prepares the calculation with the client. Significance may also depend on: • The complexity and extent of judgement required to be exercised • Whether the entity is a public interest entity • Whether the auditor originates or proposes the journal entries to record the current and deferred tax liability amounts and whether management is conversant with the tax matters sufficient to take responsibility for the accounting entries and financial statements
Apply safeguards	If the audit client is a public interest entity, the significance of the threat would be too great. The engagement is terminated or declined (Para 290.185). If the audit client is not a public interest entity, safeguards may be able to reduce the threats to an acceptable level (Section 290.184), such as: • Appointing a new person to do the calculations, or ensuring an experienced senior staff member with appropriate expertise is used to review the calculations • Using people who are not members of the audit team to perform and review the calculations

Scenario – Some accounting firms have developed their own proprietary income tax preparation software. The software is used to facilitate the preparation of company income tax returns for various tax jurisdictions. Can an accounting firm license or sell its proprietary income tax preparation software to an audit client?

The answer is generally dependent on the exact functionality of the product and whether the client will accept responsibility for preparing the return and for making significant judgements.

It sometimes happens that a client in this type of situation will defer responsibility to the software developer when 'something goes wrong'. In other situations, the client may claim that the software made significant judgements on their behalf and didn't give them the option to make appropriate decisions.

Many of these variables can be dealt with in the software license agreement. The firm should identify, evaluate and address the threats accordingly.

Scenario – A listed audit client has requested assistance in applying AASB *112 Income Taxes*.

Section 290 does address a number of situations that may be relevant. Two of these are discussed:

- Current and deferred tax calculations for the purpose of preparing accounting entries: these are prohibited for public interest entities if material to the financial statements (Paras 290.185 and 290.172).
- Providing technical assistance: this is allowed provided the auditor does not assume management responsibility (Para 290.170).

In both situations above, Para 290.169 allows the auditor and the client to engage in a dialogue which may involve the application of accounting standards or policies and the proposal of adjusting journal entries. However, management must be able to take responsibility for the application of the Income Tax accounting standard. For example, if the client's only knowledge of the Income Tax accounting standard and its application comes from the audit firm, management may not be capable of taking responsibility for any related decisions because they are not properly conversant in the application of the standard. This is particularly significant in the context of a public interest entity.

Whatever the scenario, it is evaluated on a case-by-case basis by identifying, evaluating and addressing threats to independence and relevant safeguards.

Scenario – A firm represents an audit client in a dispute with the Australian Tax Office (ATO).

Identify threats	Advocacy or self-review threat
Evaluate significance	Significance will depend on (for example): • Whether the client is a public interest entity and whether the proceedings will be conducted in public • Whether the firm provided the advice which is the subject of the dispute • The extent to which the outcome of the dispute will have a material effect on the financial statements • The extent to which the matter is supported by law or precedent • The nature of the firm's role (for example, representing the client as negotiator)
Apply safeguards	Paras 290.192 to 290.194 contain guidance on this matter. The auditor applies the framework approach to resolving the threats which could include having a tax professional, who is not involved in providing the tax services, advise the audit team and review the financial statement treatment. The auditor must avoid any situation where the firm accepts or is perceived to accept management responsibility, for example by negotiating on behalf of the client. Where representing the client in the tax dispute involves acting as an advocate for the client before a public tribunal or court and the amounts involved are material to the financial statements, no safeguards exist to eliminate or reduce the significance of the threats to an acceptable level (Para 290.193).

7.3.10 Corporate finance services

Scenario – An audit firm provided advice on a financing arrangement to an audit client during the year through the corporate finance department of the firm.

Identify threats	Self-review and advocacy threats
Evaluate significance	Significance is increased by the fact that this is an audit engagement (Section 290 applies). Significance will also depend on: • The scope of the engagement • Whether the client is a public interest entity (especially considering the 'independence in appearance' requirement) • Whether the corporate finance department made decisions for the client, authorised and/or executed the transaction • The degree and subjectivity involved in determining the accounting treatment and the extent of involvement by the corporate finance team • The materiality of the related amounts in the financial statements
Apply safeguards	Although it appears that the audit team and corporate finance team are separate, this safeguard may not be entirely sufficient to reduce the threats to an acceptable level. A further safeguard could be to engage a suitably qualified professional who was not on the corporate finance team to review the accounting treatment in the financial statement. If the corporate finance team has taken on management responsibilities, for example, by authorising and/or executing the transaction, it is unlikely the firm could accept or continue the engagement as auditor (Paras 290.162 to 290.166).

7.3.11 Valuation services

Scenario – A listed audit client has requested the firm to assist in valuing options granted to directors and officers.

Identify threats	Self-review threat
Evaluate significance	Significance may be influenced by many of the factors in Para 290.176 and is increased by the fact that the audit client is a public interest entity. Significance may also be impacted by the materiality of the valuation on the financial statements.
Apply safeguards	A firm shall not provide valuation services to an audit client that is a public interest entity if the valuations would have a material effect, separately or in the aggregate, on the financial statements on which an opinion will be expressed (Para 290.180). If the valuation will not have a material effect on the financial statements, safeguards are nevertheless required to reduce the threat to an acceptable level, such as having the valuation performed by members of the firm who are not part of the audit team. The auditor must avoid any situation where the firm accepts or is perceived to accept management responsibility, for example by proposing originating accounting entries after the valuation is complete. Furthermore, if the audit client's only knowledge about valuing options comes from the auditors, it will be difficult to demonstrate that they have accepted responsibility for the work.

7.3.12 Fees

Scenario – An audit firm performs the audit of a non-listed company and its subsidiary. The audit of the group contributes a large proportion of the total fees of the firm. For the 30 June 2012 audit, it is expected the fees will be 16 per cent of the total fees of the firm. In 2013, this is expected to be 18 per cent and the trend will likely continue in 2014. To counter the independence threats, the firm has appointed an engagement quality control reviewer and has appointed separate engagement partners for the holding and subsidiary companies.

Identify threats	Self-interest and intimidation threats
Evaluate significance	Significance may be influenced by: • Whether the client is a public interest entity • Whether the increasing proportion of the fees from the group represent an increasing reliance on the client • The extent to which the engagement partners rely on keeping these engagements
Apply safeguards	The safeguards that have been applied are consistent with those recommended in Paras 290.220 and 290.221. Additional safeguards could be relevant, especially if the client is a public interest entity. Para 290.222 introduces a new requirement for public interest entities as follows: an external pre- or post-issuance review must be conducted where the total fees from a client and its related entities represents more than 15 per cent of the total fees of the firm for two consecutive years. The review is conducted on the second of the two years. The new requirement is effective covering years beginning on or after 1 January 2012. In this example, this will be applicable in the 30 June 2014 financial year because that will be the second consecutive year after the effective date where the fees are more than the 15 per cent threshold. The decision as to whether the review is a pre- or post-issuance review is taken together with the client. The person who currently performs the quality control review could qualify to do the review if they are a member of the profession who is not a partner of the firm.

7.3.13 Contractor/consultant

Scenario – A person is contracted as a consultant to an audit firm.

The terms ‘contractor’ and ‘consultant’ are widely used with different and interchangeable meanings. For example, the terms could refer to employees, retired partners, or those engaged to offer specialist expertise to an audit firm.

The definition of ‘engagement team’ in the Code includes ‘all partners and staff performing the engagement and any individuals engaged by the firm or a network firm who perform procedures on the engagement’. Contractors and consultants could fall into this definition and the independence requirements will apply. External experts are excluded from the definition in the Code.

In addition, the Code and the Act include independence requirements that may apply to former partners and staff even if they are not contracted as a consultant to the firm.

The audit firm should develop and apply systems and procedures that enable the firm to identify and manage threats to independence, including those arising from contractors or consultants.

7.3.14 Former partner joins audit client

Scenario – A former partner of a firm has joined an audit client.

Familiarity or intimidation threats may be created and will have to be evaluated and addressed (see Paras 290.134 to 290.138). The precise nature and significance of the threats are influenced by many factors, such as:

- Whether the audit client is a public interest entity
- Whether the former partner was a member of the client engagement team
- Whether connections remain between the firm and the former partner
- The role of the former partner before leaving the firm and when joining the client
- Outstanding benefits due to the partner from the firm

In applying safeguards, there are many different requirements that must be complied with. They are summarised as follows:

Reference	Short description
ss. 324CB and 324CD	The 'general requirement' of the Act to avoid conflict of interest situations
ss. 324CF and 324CE	The 'specific requirements' of the Act that restrict the relationships of a former partner who fails an independence test and becomes an officer of an audit client
Paras 290.139 to 290.141	A specific 'cooling off' period (12 months) for key audit partners and the firm's senior or managing partner in the case of a client that is a public interest entity
s. 324CK	A five-year 'cooling off' period before a former partner can become an officer or director of a corporate audit client in circumstances where another former partner is already an officer of the client
s. 324CI	A two-year 'cooling off' period for a former audit partner becoming an officer of a corporate audit client

The independence test in Section 324CF of the Act and certain requirements of APES 110 are designed to check whether a former partner, who has an ongoing attachment to the firm, does not take on a key role with an audit client in either a financial or serving capacity. Applying the test can be particularly complex when the firm has outstanding payments remaining due to a former partner, such as a capital account or a pension payout.

It may be appropriate in certain situations for the audit firm and the former audit partner to seek professional or legal advice.

7.3.15 Power of attorney/executor

Scenario – A partner practices in an audit firm. The partner's mother has asked him to be executor of her will and has given him a power of attorney. The partner and his immediate family are likely to be beneficiaries of the estate. In the event of her death, probate is expected to take six weeks to finalise. While the partner is not specifically aware of any shareholdings his mother may have, it is possible that her portfolio includes investments in some of the audit clients of the firm.

If the partner is a member of the audit team of any of the audit clients in which his mother has a shareholding, a conflict of interest situation would arise when probate is granted under both the general and specific auditor independence requirements of the Act. This is because of the partner's beneficial interest in an investment in the audit client over which the partner has control and for which the partner is part of the audit team. If that situation arises and cannot be resolved within a 28-day period, the firm would have to resign as auditor or the partner would have to be removed from the audit team. The only remedy available to the partner and the firm could be to apply to ASIC for exemption under s. 341 of the Act. Note that even if the partner is not the appointed executor, this situation may arise during probate for any investment in an audit client of the firm where the partner is a member of the audit team.

Furthermore, holding a power of attorney may give rise to the appearance of a conflict of interest because of the control that can be exercised over the investments by the partner (except in the case of an enduring power of attorney that has not been affected).

It would be prudent for the partner to obtain more specific information about his mother's shareholdings and for the firm to apply the conceptual framework to identify, evaluate and address any threats to independence for any of the audit clients of the firm (both currently and in the event of the death of the partner's mother).

7.3.16 Other assurance engagement

Scenario – An audit firm has been asked to certify a trade certificate for a company. A partner of the firm is a director of the company.

Firstly, the firm will need to determine what is meant by 'certify a trade certificate', whether they are qualified to perform such an engagement and whether the engagement falls into the definition of an assurance engagement. If the engagement is an assurance engagement, the independence requirements of Section 291 of the Code will most likely apply. Section 291 requires a conceptual framework approach to be followed to identify, evaluate and address threats to independence.

Para 291.135 prohibits a partner of a firm from serving as a director of an assurance client.

8. Special consideration: Rotation requirements

8.1 Overview

Using the same senior personnel on an assurance engagement over a long period of time may create familiarity and self-interest threats.

The Code has established a seven-year rotation rule that applies to all key audit partners of audits and reviews of public interest entities. The new definitions of public interest entity (see Chapter 5) and key audit partner will have the effect of expanding the rotation requirements to include audit partners of some unlisted entities.

For listed entities, the Act continues to apply the more restrictive five-year rotation rules to individuals who 'play a significant role' in the audit. Limited extension is available as explained on the next page.

The Act	The Code
Five-year rotation rules (listed entities)	Seven-year rotation rule (public interest entities)
'Play a significant role' is defined as: • The individual auditor/lead auditor • The review auditor Note: refer to 8.4 'Audit enhancement' on the next page for changes introduced by the *Corporations Legislation Amendment (Audit Enhancement) Act 2012*.	A 'key audit partner' includes: • The engagement partner • The engagement quality control reviewer (EQCR) • Any other audit partner who makes key decisions or judgements on significant matters with respect to the audit. This may include any individual engaged by the firm or a network firm who performs procedures on the engagement (for example, an audit partner responsible for significant subsidiaries or divisions).

When comparing the rotation requirements of the Act and the Code, it is clear that there is an overlap at the engagement partner (individual auditor/lead auditor) and EQCR (review auditor) levels for the audits and reviews of listed entities. In this situation, the more restrictive five-year rotation rules of the Act will prevail.

8.2 Effective date

The effective date of the extended rotation requirements in the Code was 1 January 2013, with early adoption permitted. This was when the new definitions of public interest entity and key audit partner become effective for audits or reviews of financial statements for years beginning on or after 1 January 2013.

8.3 Transitional arrangements

The Code contains transitional arrangements that are designed to link the effective date to the client's year-end in the following circumstances:

Partner meets new definition of key audit partner	Timing
Partner is neither engagement partner nor EQCR	Effective for audit or review of financial statements of years beginning on or after 1 January 2013
Partner is engagement partner or EQCR and served in another key audit partner role immediately before becoming the engagement partner or EQCR and at the beginning of the first financial year beginning on or after 1 January 2012, served as engagement partner or EQCR for six or fewer years	Effective for audit or review of financial statements of years beginning on or after 1 January 2013

At the effective date, audit partners who 'play a significant role' in the audit of a listed entity (such as the individual auditor/lead auditor and review auditor) will need to ensure compliance with both the Act and the new requirements of the Code.

8.4 Audit enhancement

The *Corporations Legislation Amendment (Audit Enhancement) Act* passed on 18 June 2012 aims 'to ensure that Australia's audit quality framework continues to be in line with international best practice' said Bernie Ripoll, the Parliamentary Secretary to the Treasurer.

It allows directors the flexibility to extend the five-year auditor rotation period by up to two years, provided the audit committee is satisfied auditor independence and audit quality can be maintained.

Further, auditors must consider the Prudential Framework of Authorised Deposit-taking Institutions (ADIs) when reviewing the rotation requirements for financial institutions, insurance companies and APRA-regulated superannuation funds.

8.5 Application

The following is a broad summary of the rotation requirements for audit and review engagements. In all cases, the 'time out' or 'cooling off' period is two years:

Individual requiring rotation		Rotation requirement		
The Act (listed entities – *play a significant role*)	**The Code** (public interest entities – *key audit partner*)	**The Act** listed entities	**The Code** public interest entities – listed entities	**The Code** public interest entities (other than listed entities)
Individual auditor Lead auditor	Engagement partner	5 out of 7 years or 5 successive years***	7 years	7 years*
Review auditor	Engagement quality control reviewer (EQCR)**	5 out of 7 years or 5 successive years***	7 years	7 years*
N/A	Other audit partners who qualify as key audit partners*	7 years*	7 years	7 years*
Other partners with long association		N/A	Evaluate the significance of the threats and apply safeguards (where necessary)	

* Shaded area is effective 1 January 2013, with certain transitional arrangements.

** ASIC Regulatory Guide 187 does not consider there to be any substantive difference between the roles played by a review auditor and an EQCR in the conduct of the audit of a listed entity. However, if the EQCR is not a registered company auditor, that person will technically not be subject to the rotation requirements of the Act. In that situation, the EQCR will still be subject to the seven-year rotation requirements of the Code as a key audit partner.

*** Note the additional flexibility available to directors to extend the auditor rotation period by up to two years, provided the entity's audit committee is satisfied that auditor independence and audit quality can be maintained.

When a client becomes a public interest entity (other than due to the initial introduction of the public interest entity definition on 1 January 2013), the Code requires that the length of time that the individual has served as a key audit partner shall be taken into account in determining the timing of the rotation (Para 290.154) as follows:

Time already served as key audit partner when an audit or review client becomes a public interest entity	The Code Number of years that the individual can continue to serve as key audit partner
5 years or less	7 years less number of years already served as key audit partner
6 years or more	Maximum of 2 additional years

As a listed entity is by definition a public interest entity, this principle applies when an audit client becomes a listed entity, but the auditor would also apply the five-year rotation rule of the Act and give consideration to whether the partner has 'played a significant role' in the audit of the client before the listing.

8.6 Responsibility

The Code's rotation requirements will have a profound effect for all audit partners that qualify as key audit partners of public interest entities. The rotation requirements will no longer be limited to the engagement partner and EQCR of a listed audit engagement.

Auditors must adequately prepare for the new requirements before the effective date. As part of this preparation, they must establish procedures to adequately classify partners according to the key audit partner definition.

It is suggested that audit firms undertake their rotation planning at the same time that they establish systems to determine whether an audit client will satisfy the definition of a public interest entity. Detailed rotation schedules could be prepared, monitored and adjusted where necessary. Advice should be obtained if required and the firm should regularly evaluate the classification of its partners as key audit partners to take into account changing circumstances.

8.7 Examples

8.7.1 Key audit partner for a listed entity

Scenario – A partner has provided industry-specific consultation to the audit team, and made significant judgements for a listed entity from 2005 to 2011. The partner is considered to meet the key audit partner definition. He has never occupied the position of lead auditor or review auditor/EQCR and therefore does not 'play a significant role' in the audit in terms of the Act. The most recent year-end was 30 June 2011.

By applying the transitional arrangements, the effective date of the new rotation requirements in the Code will apply to the audit of financial statements for years beginning on or after 1 January 2013. In this example, the rotation requirements are applicable in the audit of the 2014 financial year, thereby allowing the partner to continue in the role of a key audit partner for two 'transitional' years (the 2012 and 2013 financial years).

Financial year ended 30 June	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**
Play a significant role (the Act)						N/A					
Serve as key audit partner (the Code)	✓ 1	✓ 2	✓ 3	✓ 4	✓ 5	✓ 6	✓ 7	✓ Trans.	✓ Trans.	X	X

NOTE: A partner who rotates after serving as a key audit partner is not permitted to participate in the audit, provide quality control for the engagement, consult with the engagement team or the client on technical or industry-specific issues, transactions or events or otherwise directly influence the outcome of the engagement for two years.

Scenario – A partner served as review auditor for a listed entity in 2010 and as lead auditor in 2011 and has therefore 'played a significant role' in the audit in terms of the Act for two consecutive years. The year-end is 30 June. The partner served on the audit team in another key audit partner role from 2006 to 2009 before becoming the review auditor.

The five-year rotation requirements of the Act continue to apply to this partner. However, the rotation requirements of the Code must also be complied with and consideration must be given to the seven-year requirements of the Code.

By applying the transitional arrangements, the effective date of the new rotation requirements in the Code will apply to the audit of financial statements for years beginning on or after 1 January 2013. In this example, the rotation requirements are applicable in the audit of the 2014 financial year, thereby allowing the partner to continue in the role of a key audit partner for two more years (the 2012 and 2013 financial years). After that, the partner can have no further involvement with the audit for two years.

Financial year ended 30 June	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**
Play a significant role (the Act)					✓ 1	✓ 2	✓ 3	✓ 4	X	X
Serve as key audit partner (the Code)	✓ 1	✓ 2	✓ 3	✓ 4	✓ 5	✓ 6	✓ 7	✓ Trans.	X	X

8.7.2 Key audit partner for a non-listed public interest entity

Scenario – A partner has served as engagement partner for a non-listed entity since the 2005 financial year. The current year end is 30 June 2012. Under the new definition, the entity will be classified as a public interest entity at the effective date of 1 January 2013.

When the entity meets the new definition of a public interest entity on 1 January 2013, the engagement partner has already served as a key audit partner for seven completed years. The engagement partner is required to rotate off after completing the audit of the 2012 financial year. The audit firm must make plans before the start of the 2013 financial year to replace the engagement partner so that he does not serve in a key audit partner role on the effective date. There are no transitional arrangements in this scenario.

Financial year ended 30 June	**2000-2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**
Serve as key audit partner (the Code)	✓ 2	✓ 3	✓ 4	✓ 5	✓ 6	✓ 7	✓ 8	X	X

Scenario – A partner has served as engagement partner for a non-listed entity since the 2010 financial year. The most recent year-end was 30 June 2011. The partner also served in another key audit partner role for this audit client since 2006. Under the new definition, the entity will be classified as a public interest entity at the effective date of 1 January 2013.

By applying the transitional arrangements, the effective date of the new rotation requirements in the Code will apply for years beginning on or after 1 January 2013. In this example, the rotation requirements are applicable in the 2014 financial year, thereby allowing the partner to continue in the role of a key audit partner for two more years (the 2012 and 2013 financial years). After that, the partner can have no further involvement with the audit for a period of two years.

Financial year ended 30 June	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**
Engagement partner or EQCR (the Code)					✓ 1	✓ 2	✓ 3	✓ Trans.	X	X
Serve as key audit partner (the Code)	✓ 1	✓ 2	✓ 3	✓ 4					X	X

Scenario – A partner has served as engagement partner for a non-listed entity since the 2009 financial year. The most recent year-end was 30 June 2011. The partner did not serve in any other role for this client before 2009. Under the new definition, the entity will be classified as a public interest entity at the effective date of 1 January 2013.

The key audit partner can continue to serve in that role for seven years before rotating off after the audit for the 2015 financial year.

Financial year ended 30 June	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**
Serve as key audit partner (the Code)	✓ 1	✓ 2	✓ 3	✓ 4	✓ 5	✓ 6	✓ 7	X	X

8.7.3 Entity becomes a public interest entity

Scenario – A partner serves as engagement partner for a non-listed entity from the 2008 financial year. The entity is not classified as a public interest entity when the new definition becomes effective on 1 January 2013. However, in 2014, the entity substantially increases its work force so that it is classified as a public interest entity after that year.

When a client becomes a public interest entity, the Code requires that the length of time the individual has served as a key audit partner shall be taken into account in determining the timing of the rotation (Para 290.154). By applying the requirements of Para 290.154, the partner is entitled to serve a maximum of two additional years before rotating.

Financial year ended 30 June	**2001-2012**	**2013**	**2014**	**2015**	**2016**	**2017**
Serve as key audit partner (the Code)	✓	✓	✓	X	X	✓
	5	6	7	Trans.	Trans.	1

Scenario – Consider the same example above, but the entity becomes a public interest entity because it lists its securities on 1 July 2014.

In terms of the Code, the requirements would be the same.

However, the engagement partner would also become subject to the rotation requirements of the Act. The Act's rotation requirements (s. 324DA, DB, DC and DD) do not specifically address a situation where an audit client becomes a listed entity. It would be prudent to consider the time that the engagement partner has 'played a significant role' in the audit of the client before the entity was listed when applying the Act's five-year rotation requirements. While the auditor may wish to apply for relief under the Act, the provisions of the Code do not provide for relief in this instance. Therefore the partner cannot serve any additional years and must rotate off.

Financial year ended 30 June	**2001-2012**	**2013**	**2014**	**2015**	**2016**	**2017**
Play a significant role (the Act)						✓
						1
Serve as key audit partner (the Code)	✓	✓	✓	X	X	✓
	13	14	15			1

8.7.4 Opting out

Scenario – A lead engagement partner for a listed entity has completed five years in the role, then taken one year out for the audit of the 2012 year. Can the partner return to the engagement the following year, and if so for how long?

Since the partner has been out for only one year, unless the auditor was granted relief under the Act they would have to be out for an additional year before returning to the engagement.

Members should also be mindful of the provisions of s. 324DAA of the Act introduced by the *Corporations Legislation Amendment (Audit Enhancement) Act* in terms of which the directors may extend the eligibility term of the auditor for a period of up to two successive years. The approval must be granted before the end of the five successive financial years, to enable the directors to avail themselves of the opportunity to extend the audit partner's term under the new provisions of the Act.

Financial year ended 30 June	**2007-2011**	**2012**	**2013**	**2014**
Serve as key audit partner (the Code)	✓	X	X	✓
	5	1	2	1

Scenario – The 2012 audit of a non-listed client which is a public interest entity with a 30 June year end will be the last audit of the client for the person currently serving as the lead engagement partner. The Code specifies that the firm is not independent when the lead engagement partner has served more than seven years. How should the transition be handled?

The intention of the rotation rules is to allow a lead engagement partner to finish the current audit (for example, the financial year 2012 audit). The lead engagement partner could complete the current audit, even though work would extend beyond 1 July 2012, without impairing the firm's independence. However, care must be taken to ensure that the partner is not involved in work that may be performed with respect to the first quarter or half year of the 2013 reporting period. Since some of this work may be performed simultaneously with the audit, the firm will need to carefully monitor the transition to ensure compliance with the rotation requirements.

8.7.5 Year-end and prior periods

Scenario – A public interest entity client changes its fiscal year end. As a consequence, in the year of change, its 'annual' financial statements would cover less than 12 months. How would this short period be counted in determining when the audit partner should rotate?

If the entity is required to undertake a separate financial statement audit for a shorter period, then that period constitutes a 'year' for the purposes of the partner rotation requirements. If, however, the client is not required to undertake a separate financial statement audit for the period, then that period does not constitute a year for the purposes of the rotation requirements.

Scenario – A firm accepts a new public interest entity client that had previously been audited by another firm. In the course of auditing the current period's financial statements, it was determined that the newly engaged firm should re-audit the prior two periods. For the purposes of the partner rotation provisions of the Code, does this engagement constitute one year or three years of service by the audit partners?

This constitutes one year for the purposes of determining when the partners would need to rotate.

9. Special consideration: Self-managed superannuation funds

9.1 Overview

For self-managed superannuation fund (SMSF) audits, there is no difference in the application of the independence requirements and the conceptual framework of the Code of Ethics from other types of audit engagements. The following provides some guidance and direction in applying the independence requirements and framework in the specific SMSF context. However this chapter should not be read in isolation from other chapters in this guide.

9.2 Superannuation funds as public interest entities

With effect from 1 January 2013, the Code introduces additional independence requirements for audit and review clients that are public interest entities. Auditors of superannuation funds will be required to comply with the requirements of Section 290 related to public interest entities if the fund meets the relevant definition. Chapter 5 demonstrates the application of this new definition.

SMSFs are generally not considered to be public interest entities for the purposes of the independence requirements of the Code of Ethics.

9.3 Self-managed superannuation funds (SMSFs)

There is a strong misconception that the auditor independence requirements of the Code of Ethics do not need to be applied to SMSF audit clients, largely because of their relative size. SMSFs generally fall within the 'small client' category as discussed in Chapter 4. This classification has a direct impact on the type and significance of independence threats. As an example, close relationships with a client are often more prevalent between small clients, such as SMSFs and their auditor. This can make it challenging to apply safeguards to reduce the threats to independence to an acceptable level, but it does not diminish the need for the application of the independence requirements of the Code of Ethics.

A legal requirement exists under the *Superannuation Industry (Supervision) Act 1993* (SISA) for SMSF trustees to have their fund audited annually. As a professional accountant, you are obliged to carry out such an audit in accordance with auditing standards and in compliance with the independence requirements of the Code of Ethics. This applies regardless of the size or simplicity (or level of complexity) of the SMSF or any perception that the fund is otherwise complying with other legal requirements. Furthermore, independence requirements of the Code of Ethics apply regardless of how proficiently or thoroughly an auditor may believe they can or are able to carry out an audit.

We have included discussion of instances where independence may need to be considered as a consequence of relationships with the client away from the audit client themselves; for example the source of the referral of audit work may lead to auditor independence concerns. This may include the relationship with the referral source or the volume of work being received from one referral source.

If an SMSF auditor has any doubt about their independence in carrying out an audit and they are unable to put appropriate safeguards in place, they should decline the audit engagement. As part of the process in assessing independence, auditors may consider as a 'litmus' test, asking themselves if they would have any hesitation in writing up an adverse finding or in qualifying an audit report. If there is any hesitation, it may be an indication that independence is impaired and consideration should be given to declining the audit engagement.

9.4 Examples

The examples that follow are intended to deal with common independence issues that arise in practice. The factors that impact the significance of a threat to independence and the safeguards proposed are only examples. In all situations, members must be mindful of their professional obligations to act in the public interest and, in particular, whether a situation could pass the 'independence in appearance' test. Auditors should seek advice from their professional accounting body where necessary.

It is the view of the professional accounting bodies that there are some scenarios involving SMSFs in which independence requirements would be breached. In each of these cases, it would be expected that an auditor would decline an audit engagement.

1. An auditor cannot audit an SMSF where the individual auditor has significantly prepared the accounts for the SMSF (APES 110, Sections 290.168 and 290.171)
2. An auditor cannot audit an SMSF where staff reporting directly to them have prepared the accounts (APES 110, Sections 290.162, 290.163 and 290.171)
3. An auditor cannot audit their own SMSF (APES 110, Sections 290.102 and 290.146)
4. An auditor cannot audit the SMSF where a partner within their own firm is a member/trustee of that SMSF (APES 110, Sections 290.124 and 290.146)
5. An auditor cannot audit the SMSF where a relative or a related party of the auditor is a member/trustee of that SMSF or where the auditor has a close personal relationship (APES 110, Section 290.127) or business relationship with a member/trustee of the SMSF (APES 110, Section 290.124). Reference to SIS Act definitions for relatives and related party should be considered

An auditor cannot audit an SMSF where they or their staff have prepared the accounts

Some confusion arises about the meaning of paragraph 290.171 of APES 110, which refers to 'services related to the preparation of accounting records and financial statements' being provided to 'an audit client that is not a public interest entity, where the services are of a routine or mechanical nature'. As an example of such services, the paragraph identifies 'preparing financial statements based on information in the trial balance'.

The paragraph refers to applying safeguards 'when necessary' to eliminate the self-review threat or reduce it to an acceptable level. Examples of safeguards are given as:

- Arranging for such services to be performed by an individual who is not a member of the audit team; or
- If such services are performed by a member of the audit team, using a partner or senior staff member with appropriate expertise who is not a member of the audit team to review the work performed.

It is the view of the joint accounting bodies that, in the context of the audit of SMSFs, it would always be necessary as a minimum to apply such safeguards.

However, we consider that the scenario contemplated by paragraph 290.171 does not permit an individual auditor to take full professional responsibility for the preparation of an SMSF's financial statements, and then to provide an audit report on those financial statements. The paragraph contemplates a minimal or restricted set of services ('of a routine or mechanical nature') requiring only a minor review (because of their nature). Where an accountant takes full professional responsibility for the preparation of financial statements for an SMSF, in a manner which legally binds the accountant to the statements produced, and where the accountant would be responsible at law for rectifying any defects, then the self-review threat which arises, were that same accountant to undertake an audit of those financial statements, would be so great that no safeguard could reduce the threat to an acceptable level.

On this basis, a sole practitioner or their staff would be unable to both prepare the financial statements and audit them, as they would of necessity be taking full professional responsibility for both services.

An auditor cannot audit their own SMSF

Paragraph 290.146 of APES 110 provides that, if a partner or employee of the firm serves as a director or officer of an audit client, the self-review and self-interest threats created would be so significant that no safeguards could reduce the threats to an acceptable level. Therefore, where a person is a member and trustee of an SMSF, that person would be unable to conduct the audit of that SMSF. Note that APES 110 defines 'director or officer' to mean 'those charged with the governance of an entity, or acting in an equivalent capacity, regardless of their title', and the term therefore covers the individual trustees of an SMSF, or the directors of a trustee company.

An auditor cannot audit the SMSF where a partner within their own firm is a member/trustee of that SMSF

Also by application of the provisions in paragraph 290.146, no audit can be undertaken of an SMSF in which a partner (or employee) of the auditor is a member or trustee of the SMSF. Note that 'partner' should not be read in the narrow sense of a partnership at law. Although 'partner' is not a defined term in APES 110, it is used extensively in the professional standards issued by the APESB, and is defined in APES 320 *Quality Control for Firms* as 'any individual with authority to bind the Firm with respect to the performance of a Professional Services Engagement'. It should be read similarly in the context of paragraph 290.146, and would apply to directors of a corporate entity and trustees of a trust, in addition to partners of a partnership.

Not all scenarios are clear cut when determining whether appropriate safeguards are in place to meet professional obligations around independence. The following seeks to provide guidance on some common scenarios.

9.4.1 'The books' are prepared by the auditor

Scenario – The auditor of an SMSF is asked to prepare the accounting records and/or the financial statements of the fund. This may include, for example, recording the transactions when the fund has very few transactions, preparing the general ledger and trial balance, and proposing and posting journal entries. No advice is given in relation to the accounts.

The approach to this question is the same as in the scenarios in example one of Chapter 7. However, in each case, the significance of the identified threats and the safeguards that are applied will be influenced by factors such as:

- The required specialised knowledge or competency that may be necessary to undertake the engagement
- Skills, knowledge and experience of the trustee who prepared the accounts
- The existence of relationships between the auditors and the members and trustees of the fund

The general principles that continue to apply are:

- For entities that are not public interest entities such as SMSFs, the auditor can provide services related to the preparation of accounting records and financial statements that are routine and mechanical in nature and provided the

self-review threat is reduced to an acceptable level (APES 110, Section 290.171). However, care needs to be exercised to ensure that appropriate safeguards are in place to mitigate possible breaches of independence requirements.

- Auditors must exercise their professional judgement in determining how the extent of their involvement in accounts preparation will impact their independence in carrying out an audit. For example, if the SMSF trustees had prepared the accounts and the auditor filled in pro-forma financial statements based on the trustees' work, audit independence is less likely to be impaired. However, if the auditor undertakes tax calculations or provides advice to the trustee on how to prepare the accounts, then it is not likely that the independence requirements can be met.

9.4.2 Carrying out the accounting/tax role and audit function in the same firm

Refer also to Chapter 7 for examples of common independence issues.

Scenario – A partner within an accounting firm is responsible for the preparation of an SMSF's accounts and tax returns. Another partner within the same firm is assessing whether to accept the audit engagement for the SMSF.

This particular scenario is common for professional accountants in public practice, and for many firms the decision is made to outsource the audit function to avoid any issues with independence.

Larger firms will normally find it easier to put appropriate safeguards in place to ensure that independence principles can be adhered to in carrying out an SMSF audit in addition to preparation of accounts. Smaller firms, however, will find this challenging.

Often referred to as 'Chinese walls', it is possible for a firm to carry out both the accounting/tax work and audit work for an SMSF client, but only with appropriate safeguards in place to ensure audit independence. If the safeguards can not be put in place, the firm will need to decline the audit engagement and outsource the audit function.

Basically, where segregation of the actual roles and responsibility for the preparation of the financial statements, and the audit of the financial statements exists, auditor independence should not be impaired. It is often what constitutes segregation of duties that causes much uncertainty and where SMSF auditors may struggle to ensure they meet their professional obligations.

Where a firm has separate business divisions carrying out the different roles with distinctly different reporting lines to partners within those divisions, it could be possible for this arrangement to establish an appropriate safeguard and for the auditor to be able to meet their professional obligations. Typically, this would involve a business services division (or SMSF administration services division) and a separate audit division. Staff within each division would carry out the work reporting to the partner of each of those divisions.

Smaller firms with two or three partners would find it difficult to put appropriate safeguards in place. Example one in Chapter 7 covers appropriate safeguards that could be put in place such that both the audit and accounting function are able to be carried out in the same firm. In that example, the appropriate safeguards would entail the client taking explicit responsibility for the financial statements and any adjustments that the firm makes. In an SMSF context it would be difficult to see how these safeguards could actually work in practice, unless the firm is able to demonstrate their assessment that the SMSF trustee had sufficient knowledge of the accounts and any changes, to truly be in a position to take responsibility for them; and that in fact the trustee did take responsibility for them.

As discussed above, a sole practitioner would not be able to audit an SMSF for whom they have undertaken the accounts preparation. Appropriate safeguards could not be put in place to avoid the self-review threat.

Scenario – A staff member within a sole practitioner accounting firm is responsible for the preparation of an SMSF's accounts and tax returns. The sole practitioner principal of the firm is assessing whether to accept the audit engagement for the SMSF.

Example one in Chapter 7 discusses similar arrangements for small audit engagements. In an SMSF context, the same principles apply.

Sole practitioners would not be able to put appropriate safeguards in place as all of their staff are essentially reporting to them, and there is no opportunity within the practice to segregate ultimate responsibility for the audit engagement from the non-assurance services. It is not relevant that different staff are carrying out each separate function or that a staff member prepares the accounts that are then audited by the partner. It does not matter if the partner had no role in the preparation of the accounts. The issue is that the reporting mechanisms within the firm are such that all staff ultimately report to the sole practitioner (auditor). Similarly, it would not suffice for the sole practitioner to prepare the accounts which were then audited by a staff member.

These practitioners would need to outsource the audit function for their SMSF clients.

Scenario – An accounting firm acts as tax agent for an SMSF. They assist the SMSF client in preparing the return and tax calculations for which the client takes responsibility. The auditor (another partner in the firm) is assessing whether to accept the audit engagement for the SMSF.

APES 110, Section 290.183 addresses the issues of tax return preparation. Where the client takes responsibility for the SMSF annual return, including any significant judgements made, it is generally not considered to create a threat to independence.

Auditors need to be careful, however, when other tax services are provided to the client. APES 110, Sections 290.181 and 290.182 clearly state that the provision of certain other tax services may pose a threat to auditor independence. Auditors will need to consider a range of factors in determining whether appropriate safeguards can be put in place to overcome any risks, including the complexity of any tax advice given and the level of tax expertise of the client's employees who are receiving the advice.

9.4.3 Carrying out an SMSF audit as a consultant, ex-partner or ex-employee of a firm

Scenario – An auditor has been approached to conduct the audits for clients of a firm providing accounting/tax services to SMSF clients. The auditor is a consultant, ex-partner or former employee of that firm.

After a staff member leaves a firm or a partner retires, they are sometimes asked to undertake the audit role for the firm's SMSF clients. Some firms may see this as outsourcing their SMSF audit clients to a third party and therefore relieving themselves of any issues that may arise around independence for those clients.

However, prior to accepting the audit engagement, those ex-partners or ex-employees still need to assess their independence in relation to the client and the firm, even though they are not associated with the firm as a partner or employee at the time they undertake the audit. Threats may still exist around familiarity and self review if the partner or employee had previously worked on or advised that client, particularly if little time has passed since working for the firm.

In such circumstances, the auditor may not be able to put appropriate safeguards in place to guard against threats and would therefore need to decline the audit engagement.

What is important to understand is that outsourcing SMSF audit activity does not guarantee independence. An auditor must assess their independence on each and every audit engagement, giving consideration to a range of factors aside from the client relationships at the time the audit is being undertaken.

9.4.4 Relationships between auditors and referral sources

Referrals of SMSF audit clients will often come from accountants rather than appointments arising from individual trustees. These types of referral arrangements will need to be considered in light of independence requirements. This is despite the fact that the subsequent appointment or engagement is with the SMSF trustee.

Where a large percentage of an SMSF auditor's work comes from one referral source, dependence on that referral source and possible concerns centred on retention of the audit clients may create a threat to independence. The Code of Ethics requires auditors to evaluate the threat and apply safeguards where necessary to eliminate the threat or reduce it to any acceptable level. This may include reducing the dependency on the external accounting practice (source of audit client referrals), external quality control reviews or external consultation on key audit judgements. APES 110, Sections 290.220 and 290.221 specifically address the issue of fees and the appropriate safeguards that could be put in place where a firm receives a large proportion of its fees from one source.

The threat to independence may be further exacerbated if that referral source is a former employer. SMSF auditors need to consider whether there is a self-review threat in auditing an SMSF to which they may have provided services at a previous employer.

Furthermore, the relationship between the auditor and the referral source may need to be considered in light of independence requirements. A close personal or business relationship with the referral source may pose risks for auditors.

Scenario – An auditor is asked by an administration firm to accept the audit work of multiple SMSF clients. The fees generated from this work would effectively double the fee base of the auditor.

Although the audit engagement is an arrangement between the auditor and the SMSF trustees, the reality is that a number of clients have been referred from one source. Consequently the auditor will need to consider the possible impact of reliance on one referral source on auditor independence. This arrangement could lead to a self-interest or intimidation threat. It is possible for the perception of impaired auditor independence to arise. For example, it may lead to the auditor being reluctant to issue an adverse finding on one of the clients, because of the risk of losing all the clients from the one referral source. Remember, an auditor must be independent in both fact and appearance.

SMSF auditors who find themselves in this situation may need to decline some or all of the audit work to either eliminate the threat or reduce it to an acceptable level.

Scenario – An auditor is asked by an accounting firm to accept the audit work of their SMSF clients. The principal in the accounting firm is the auditor's son.

Although each audit engagement is with an individual SMSF audit client, a perception may exist that the auditor is not independent in carrying out the audit. Consider, for example, in a situation where the auditor may contemplate an adverse finding on a client that ultimately may reflect badly on the auditor's son. In some situations, for example a blatant breach by the client, the auditor may not be reluctant to qualify an audit report, but if the breach occurred due to an error on the part of the accountant (the auditor's son), some reluctance may exist. In these cases, the perception of independence would be questioned.

9.4.5 Firms offering financial advisory services

Financial advisory services can offer a particular independence challenge for firms where they wish to offer SMSF audit services to the same client. The remuneration structure the firm uses in charging for the financial advice they provide may place an auditor at particular risk of a breach in independence principles, however it is not the only factor that needs to be considered.

Where a firm is receiving remuneration under structures such as commissions or asset based remuneration, it would be difficult for appropriate safeguards to be put in place to overcome threats to independence. This is largely because the auditor's income is directly linked to the financial advice given. Under these models, an auditor would need to consider declining the audit engagement.

A genuine fee for service model may be seen as an appropriate safeguard for an auditor. However, an auditor would still need to approach independence in a similar manner as when the firm offers tax or accounting services (discussed above). Regardless of the remuneration structure, it is important to note that similar assessments will still need to be made as outlined in Example two where the firm is offering other services to the client. Appropriate safeguards will need to be implemented to reduce to an acceptable level or eliminate independence risks if the firm is to accept the audit engagement. Particular attention may need to be paid to the types of financial advisory services including where product recommendations are made.

There is no exhaustive list of the types of scenarios in which financial services may pose a particular problem for an auditor in putting appropriate safeguards in place. In most cases, it will be very difficult for an auditor to put appropriate safeguards in place and in those cases the firm would need to outsource the audit function. Even if the firm ceases to offer financial advisory services, an auditor would still be facing the same risks, as effectively they would still be auditing the firm's work in subsequent years while product recommendations and investment decisions remain in place.

Scenario – A partner within a firm that offers financial advisory services is assessing whether to accept the audit engagement for an SMSF to whom financial advisory services are supplied.

If an auditor is assessing the compliance or validity of a particular product or investment arrangement that has been recommended or implemented by the firm, it may be perceived that the auditor would not be independent in undertaking their role. For example, if a limited recourse borrowing arrangement has been recommended and set up for an SMSF client by the firm, the auditor may not be independent in making an assessment of whether the arrangement is compliant or has been correctly set up. Despite the fact that they may be extremely knowledgeable about such arrangements, a reasonable person may not perceive them as being independent in making that assessment. It is the absence of independence (or perception of independence) that would require the auditor to decline the audit engagement in this circumstance.

10. Independence communications

10.1 Overview

The Code and the Act contain specific requirements for auditors to communicate regarding independence, both within the firm and with those responsible for governance. Even when it is not required, regular two-way communication on independence between the auditor and those charged with governance of an audit client is encouraged and would represent best practice.

10.2 Auditor's independence declarations

In the case of entities audited in accordance with the Act, the auditor shall make a written declaration to the client that there have been no contraventions of the independence requirements, or if there have been, that they have been set out in the written statement. Such a declaration is given in terms of s. 307C of the Act.

ASA 260 *Communication with Those Charged with Governance* further mandates for listed entities the specific requirement for the auditor to communicate:

- A statement that the engagement team and others in the firm, and network firms where appropriate, have complied with the independence requirements
- All relationships and matters that may reasonably be thought to bear on independence, including total fees charged during the period for audit and non-audit services provided by the firm and network firms to the entity and components it controls (allocated to categories that are appropriate)
- The related safeguards that have applied to eliminate identified threats or reduce them to an acceptable level

Template 1 could be used or amended to comply with these requirements.

The entities for which a declaration under s. 307C is required are shown in the table below:

	Type of entity	**Is an independence declaration under s. 307C required for an audited or reviewed financial report?**
CORPORATIONS ACT 2001	**Disclosing entity** where the financial report is required under Chapter 2M	**Yes**
	Public company where the financial report is required under Chapter 2M	**Yes**
	Large proprietary company where the financial report is required under Chapter 2M	**Yes**
	Registered scheme where the financial report is required under Chapter 2M	**Yes**
	Small proprietary company where the financial report is required under Chapter 2M pursuant to a direction by shareholders or from ASIC	**Yes**
	Small proprietary company under foreign company control that prepares a financial report under s. 292(2)(b)	**Yes**
OTHER	**Financial services licensee** where the financial report is required under Chapter 7	No, unless the licensee is also required to prepare the financial report under Chapter 2M
	Superannuation fund	No, as superannuation funds prepare accounts in accordance with the SIS Act and Financial Services (Collection of Data) Act.

10.3 Independence confirmations

Under ASQC1 paragraph AUS 24.1, the firm shall obtain written confirmation of compliance with its policies and procedures on independence from all firm personnel that are required to be independent at least annually.

A similar written confirmation from each member of the assurance team may be a useful tool to help an engagement partner evaluate compliance with independence requirements on an engagement. Likewise, inter-firm declarations can be used where other firms perform the audit of subsidiaries that will form part of the audit of a group. Auditing Standard ASA 600 *Special Considerations – Audits of a Group Financial Report (Including the Work of Component Auditors)* provides further guidance.

Templates 2, 3 and 4 below could be used or amended for these purposes. None of the templates cover the independence requirements of other jurisdictions (for example, SEC requirements).

10.3.1 Template 1 – Auditor's independence declaration (s. 307 of the Act)

[Addressed to the audit client]

Dear [ ]

[Insert Name of company/entity]

We have [audited/reviewed as appropriate] the financial statements of [Name of company/entity] for the financial period ended [insert half-year or year-end date].

As lead engagement [partner/auditor] for the [audit/review] engagement, I declare that, to the best of my knowledge and belief, there have been:

- no contraventions of the independence requirements of the *Corporations Act 2001* in relation to the [audit/review]; and
- no contraventions of any applicable code of professional conduct in relation to the [audit/review].

OR

As lead [engagement partner/auditor] for the [audit/review] engagement, I declare that, to the best of my knowledge and belief, the only contraventions of the independence requirements of the *Corporations Act 2001* in relation to the [audit/review], and any applicable code of professional conduct in relation to the [audit/review], are set out below:

.....

[Name of auditor] [Location]

Partner

Name of firm [Date]

10.3.2 Template 2 – Sample annual independence confirmation

[Date]

[Addressed to the firm]

Dear [ ]

Annual written confirmation

I have read and understand the firm's policies and procedures relating to ethical requirements. To the best of my knowledge, I confirm that I am compliant with the firm's policies and procedures relating to ethical requirements, including the independence requirements for assurance clients.

[I am aware of my responsibility to promptly inform the firm if I become aware of any threat, or suspected threat, that may indicate the firm's policies and procedures relating to ethical requirements are not being complied with.]

[Name and signature]

[For listed entities, or any other audit review client if deemed appropriate, the following paragraphs may be appended to the letter in order to comply with ASA 260:]

I declare … that …

- the firm, [network firms,] the engagement team and others in the firm have complied with relevant ethical requirements regarding independence;
- I/we have communicated to you all relationships and other matters that in my/our professional judgement may reasonably be thought to bear on independence (including a categorisation of fees to assist you in assessing the effect of our non-audit services on our independence);
- I/we have communicated to you the safeguards that have been applied to eliminate identified threats to independence or reduce them to an acceptable level [including details of remedial action taken or proposed in the case of inadvertent violation of relevant ethical requirements].

10.3.3 Template 3 – Sample assurance team member confirmation

Date]

[Addressed to the firm]

Dear [ ]

Independence confirmation: [Audit/Review/Assurance as appropriate] Engagement of [Name of client] and its [controlled/ related entities] for the period ended [insert period end date]

I acknowledge that I will be part of the [audit/review/assurance as appropriate] team for the above mentioned engagement.

I am familiar with the firm's policies and procedures relating to independence for [audit/review/assurance as appropriate] clients. To the best of my knowledge, I confirm that I am not aware of any circumstance or relationship that could impair or be seen to impair my independence with regard to this engagement.

In particular:

- Neither I, nor any of my immediate family, owe any amount to the client other than amounts that arose in the ordinary course of business and in accordance with normal terms and conditions;
- Neither I, nor any of my immediate family, have any direct or indirect financial interests or relationships with the client;
- [add other as required]

I will promptly inform the engagement partner if there is any change to any of my assertions in this letter.

[Name and signature]

11. Appendices

Appendix 1 – Applicable independence standards

Standard/Legislation/Regulation	Operative date	Issued by	Website
APES 110 *Code of Ethics for Professional Accountants* – the Code is mandatory for members of the professional bodies and supersedes APES 110 that was issued in June 2006 and subsequently amended in February 2008	Issued December 2010 Operative 1 July 2011 Amended December 2011* * Requirements relating to public interest entities and rotation of key audit partners are effective from 1 January 2013	APESB	www.apesb.org.au
ASA 102 Compliance with Ethical Requirements when Performing Audits, Reviews and Other Assurance Engagements – establishes requirements for compliance with relevant ethical requirements	For reporting periods commencing on or after 1 January 2010	AUASB	www.auasb.gov.au
APES 320 Quality Control for Firms – requires firms to establish a system of quality control (including relevant ethical requirements)	In effect	APESB	www.apesb.org.au
ASCQ 1 Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, and Other Assurance Engagements – requires firms to establish a system of quality control (including relevant ethical requirements)	In effect	AUASB	www.auasb.gov.au
ASA 220 Quality Control for an Audit of a Financial Report and Other Historical Financial Information – includes specific responsibilities for ethical requirements and related documentation	For reporting periods commencing on or after 1 January 2010	AUASB	www.auasb.gov.au
Framework for Assurance Engagements – describes the elements and objectives of an assurance engagement and identifies engagements to which the AUASB standards apply	19 April 2010** ** Supersedes the Framework for Assurance Engagements issued in June 2007	AUASB	www.auasb.gov.au
ASA 260 Communication with Those Charged with Governance – includes requirements for communicating on matters of independence	For reporting periods commencing on or after 1 January 2010	AUASB	www.auasb.gov.au
Corporations Act 2001 – includes sections relevant to auditor independence for the audit and review of full-year and half-year financial reports*** *** The provisions are contained mainly in s. 307C and Divisions 3, 4 and 5 of Part 2M.4. Division 5 contains the requirements for auditor rotation for listed companies	In effect	Commonwealth Government	www.comlaw.gov.au

Standard/Legislation/Regulation	Operative date	Issued by	Website
Regulatory Guide 187 Auditor Rotation – includes the interpretation of the legislation relating to auditor rotation for listed entities and specifies how ASIC will regulate it	In effect	ASIC	www.asic.gov.au
Prudential Regulatory Standards – These prudential regulatory standards include certain provisions dealing with the independence requirements for auditors and are consistent with the *Corporations Act 2001*: • APS 510 Governance – applicable to authorised deposit-taking institutions • GPS 510 Governance – applicable to general insurance companies • LPS 510 Governance – applicable to life insurance companies	In effect	APRA	www.apra.gov.au

Appendix 2 – Applicable independence standards (by entity classification and type of engagement)

Applicable independence standards

Classification of entity	Type of engagement	Outcome	Applicable section of the Code	Applicable corporate legislation	Other applicable regulation
Public interest entity	Audit and review engagements	Annual and half-year financial reports/ statements	Section 290	*Corporations Act 2001* Divisions 3,4 and 5 of Part 2M.4 and s. 307C	*ASIC Regulatory Guide 187 Auditor Rotation (For Listed Entities)* APS 510 *Governance (For Authorised Deposit-Taking Institutions)* GPS 510 *Governance (For General Insurance Companies)* LPS 510 *Governance (For Life Insurance Companies)*
		Other historical financial information			
	Other assurance engagements		Section 291		
Not a public interest entity	Audit and review engagements	Annual and half-year financial reports/ statements	Section 290	*Corporations Act 2001* Divisions 3 and 4 of Part 2M.4 and s. 307C	
		Other historical financial information			
	Other assurance engagements		Section 291		