

Draft Query of the week – Auditor Independence Declarations

Q: When is an auditor required to provide a written independence declaration?

A: Auditors have both professional and legal obligations to communicate in writing regarding their independence and are required to comply with both the spirit and letter of the law. While similar, the specific requirements of the professional standards and the law do differ in detail.

The Code of Ethics APES 110 adopts a conceptual framework that requires the identification and evaluation of threats to independence and, where possible, the application of safeguards to eliminate or reduce any threats created to an acceptable level.

The Corporations Act itself includes both a general independence requirement and also specific independence requirements concerning financial and other relationships. The general requirement concerns conflict of interest situations where:

- (a) The auditor, or a professional member of the audit team, is not capable of exercising objective and impartial judgment in relation to the conduct of the audit of the audited body; or
- (b) A reasonable person, with full knowledge of all relevant facts and circumstances, would conclude that the auditor, or a professional member of the audit team, is not capable of exercising objective and impartial judgment in relation to the conduct of the audit of the audited body.

There can be circumstances that contravene the independence requirements of the Act itself that do not contravene the requirements of APES 110. Conversely, there can be circumstances that contravene the requirements of APES 110 that do not contravene the requirements of the Act.

In summary then:

1. The relevant provisions of the Code of Ethics APES 110, section 290 Independence – Assurance Engagements provides that:

290.30 Firms should establish policies and procedures relating to Independence communications with audit committees, or others charged with governance of the client. In the case of Listed Entities, disclosing entities and registered schemes the Firm should communicate orally and in writing, for each financial and half year report, all relationships and other matters between the Firm, Network Firms and the Audit Client that in the Firm's professional judgment may reasonably be thought to bear on Independence. Matters to be communicated will vary in each circumstance and should be decided by the Firm, but should generally address the relevant matters set out in this section and must include a written statement that, to the best of the knowledge and belief of the Lead Engagement Partner there have been no contraventions of the Independence requirements of this Code.

2. Corporations Act 2001 Section 307C(1) provides:

Draft Query of the week – Auditor Independence Declarations

If an individual auditor conducts:

(a) an audit of the financial report for a financial year; or

(b) an audit or review of the financial report for a half-year;

the individual auditor must give the directors of the company, registered scheme or disclosing entity:

(c) a written declaration that, to the best of the individual auditor's knowledge and belief, there have been:

(i) no contraventions of the auditor independence requirements of this Act in relation to the audit or review; and

(ii) no contraventions of any applicable code of professional conduct in relation to the audit or review; or

(d) a written declaration that, to the best of the individual auditor's knowledge and belief, the only contraventions of:

(i) the auditor independence requirements of this Act in relation to the audit or review; or

(ii) any applicable code of professional conduct in relation to the audit or review;

are those contraventions details of which are set out in the declaration.

More detail follows

Where an entity is required to prepare a financial report in accordance with Chapter 2M of the Corporations Act then an 'Auditor Independence Declaration' is required by s. 307C. Entities required to report under Chapter 2M are:

- Disclosing entity;
- Public company;
- Large proprietary company;
- Registered scheme;
- Small proprietary company where shareholders direct the company to provide an audited financial report under s. 293;
- Small proprietary company directed to provide an audited financial report by ASIC under s. 294; and
- Small proprietary company under foreign company control that prepares a financial report under s.292(2)(b).

In summary then, to determine whether an Independence Declaration is mandatory consider both of the following questions for each type of audit client for annual and half year audits and reviews (where applicable).

Draft Query of the week – Auditor Independence Declarations

CHAPTER 2M								OTHER	
Is an Independence Declaration under s. 307C required for an audited financial report of a	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? Yes	small proprietary company where the financial report is required under Chapter 2M pursuant to an ASIC direction? Yes	small proprietary company under foreign company control that prepares a financial report under s.292(2)(b)? Yes	financial services licensee where the financial report is required under Chapter 7? <i>No, unless the licensee is also required to prepare the financial report under Chapter 2M.</i>	superannuation fund? <i>No, as superannuation funds prepare accounts in accordance with the SIS Act and Financial Services (Collection of Data) Act.</i>
Is written communication with an audit client required under APES 110 Para. 290.30 for an audited financial report of a	disclosing entity ¹ ? Yes. This communication may be included in the Independence Declaration under s. 307C, but it may be necessary to include additional information to	²	²	registered scheme? Yes. This communication may be included in the form of an Independence Declaration under s. 307C, but it may be necessary to include additional	²	²	²	²	²

¹ A disclosing entity includes a listed entity (s. 111AE)

² APES 110 Para 290.30 only requires written communication for listed entities, disclosing entities and registered schemes

Draft Query of the week – Auditor Independence Declarations

	that required by the Act itself.			information to that required by the Act itself.					
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Refer to APES 110 Section 290 Appendix for a pro forma Independence Declaration