



Australian Government

Financial Reporting Council

FINANCIAL REPORTING COUNCIL ANNUAL REPORT 2016-17

**FINANCIAL
REPORTING
COUNCIL
ANNUAL
REPORT
2016-17**

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Australian Government
Financial Reporting Council

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28 September 2017

The Hon Scott Morrison
Treasurer
Parliament House
CANBERRA ACT 2600

Dear Treasurer

I have pleasure in presenting the annual report of the Financial Reporting Council (FRC) for the year ended 30 June 2017.

The report has been prepared in accordance with sections 235B of the *Australian Securities and Investments Commission Act 2001* (ASIC Act) for presentation in the Parliament. Subsection 235B(1) of the ASIC Act requires the FRC to prepare a report on its operations during the year, and on the achievement of the objects of Part 12 of the ASIC Act relating to accounting and auditing standards. Section 225(2B) of the ASIC Act further requires the FRC to provide strategic policy advice and report on the quality of audits conducted by Australian auditors.

Subsection 235B(4) of the ASIC Act requires the report to be tabled in each House of the Parliament as soon as practicable.

Yours sincerely

A handwritten signature in black ink that reads 'Bill Edge'.

Bill Edge
Chair

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Chair's report

In 2016-17 the Financial Reporting Council (FRC) continued to oversee the effectiveness of the Australian financial reporting framework and the processes for setting accounting and auditing standards, including providing strategic advice in relation to the quality of audits conducted by Australian auditors.

Based on the activities outlined in this annual report, the only specific action that the FRC recommends the Minister take is to support, and encourage others to support, initiatives to improve the financial reporting system according to Strategic Priority number 1 of the FRC

Strategic Plan 2017-20 (see below).

FRC Strategic Plan 2017-20

During the year the FRC approved its Strategic Plan for 2017-20, which outlines six Strategic Priorities:

1. To promote initiatives to improve the financial reporting system for both the public and private sectors (including the not-for-profit sector as well as the for-profit sector) and to make financial reports more useful, simple and relevant.
2. To continue to monitor the quality of audits carried out by Australian auditors.
3. To continue to influence international accounting and auditing developments, particularly by promoting suitably qualified Australians and New Zealanders for appointment to relevant international boards.
4. To consider external reporting initiatives including their alignment with, and impact on, financial reporting requirements.

5. To continue and enhance interaction with stakeholders, including users, preparers and auditors of financial reports.
6. To encourage appropriate use of technology in the preparation and auditing of financial reports.

Stakeholder engagement

The FRC considers it essential that regular contact be made with all stakeholders in the capital markets, and we continue to maintain and strengthen our communication with them.

We thank those stakeholders who regularly communicate with us, particularly:

- Association of Superannuation Funds of Australia (ASFA);
- Australian Charities and Not-for-profits Commission (ACNC);
- Australian Council of Superannuation Investors (ACSI);
- Australia Institute of Company Directors (AICD);
- Australian Prudential Regulation Authority (APRA);

- Australian Securities and Investments Commission (ASIC);
- Australian Securities Exchange (ASX);
- Australian Shareholders' Association (ASA);
- Business Council of Australia (BCA);
- Chartered Accountants Australia and New Zealand (Chartered Accountants ANZ);
- CPA Australia;
- Department of Finance;
- External Reporting Board of New Zealand (XRB);
- Financial Services Council (FSC);
- Governance Institute;
- Group of 100 (G100);
- Institute of Internal Auditors-Australia (IIA);
- Institute of Public Accountants (IPA);
- Heads of Treasuries Accounting and Reporting Advisory Committee (HoTARAC); and
- The Treasury.

The number of stakeholders listed above indicates the broad range of participants and accordingly, issues that impact on the financial reporting system.

Standards oversight

One of the FRC's key functions is to oversee the process for setting accounting and auditing standards in Australia. The FRC acknowledges the considerable work undertaken by the Australian Accounting Standards Board (AASB) and the Auditing and Assurance Standards Board (AUASB) during 2016-17. Their specific achievements and ongoing work are reported separately in their respective annual reports, which I encourage stakeholders to read.

Changes to the FRC membership

As reported last year the FRC membership was reduced to ten with the aim of enabling the FRC to act with greater agility and efficiency.

This is the first year of the reconstituted membership, and as this annual report reflects, has been a successful year. Two members, Kevin Lewis and David Nicol, were reappointed for a further three year term. I congratulate them and appreciate the continuity of membership their reappointments enable.

Furthermore, the newly appointed AUASB Chair, Professor Roger Simnett AO, was also appointed to the FRC and we look forward to his ongoing contribution.

Outgoing AUASB Chair, Merran Kelsall, also retired from the FRC and the FRC paid tribute to the extraordinary and noteworthy contribution she made to standard setting in Australia and internationally.

Review of IFRS adoption in Australia

A significant activity of the AASB during the year was to review the implementation of International Financial Reporting Standards (IFRS Standards) since their adoption in Australia in 2005.

The overall feedback from stakeholders suggests that the adoption of IFRS Standards was generally positive for the Australian economy, although complying with the IFRS Standards-based AASB standards is challenging for some entities, particularly NFP entities.

The FRC is satisfied with the process undertaken, the conclusions reached and the proposed actions.

International developments

The FRC monitors international developments to ensure the Australian financial reporting framework represents world's best practice.

It is also essential that Australia is influential with all international boards and committees that produce international standards and other regulation and guidance.

The FRC is particularly pleased that Professor Ann Tarca, a past AASB member, has been appointed to the International Accounting Standards Board (IASB).

Public Interest Oversight Board (PIOB)

During the year, the PIOB requested submissions on its 2017-19 Strategy.

The FRC made a submission which supported the current standing setting model and rejected implications that technical members (or those affiliated with the accounting profession) cannot be assumed to be setting standards in the public interest. The FRC stated that it particularly would not like the issue of public interest to override the need to have sufficient technically competent members.

The FRC understands that dialogue continues between various stakeholders regarding the PIOB Strategy and the FRC continues to monitor its progress.

Statutory obligations

Each year the FRC conducts a review of its performance against the obligations required of it under the Australian Securities and Investments Commission Act 2001 (ASIC Act). Our review this year confirmed that the FRC continues to satisfy all of its statutory obligations.



Mr Bill Edge

Chair
Financial Reporting Council

28 September 2017

FRC members, Treasury and XRB representatives



Back row: Alyce Reid (Treasury), Kate Phipps (Treasury), Warren Allen (XRB), Jackie Callaway, David Nicol, Noelle Kelleher, Richard Grant (Treasury)

Front row: Graeme Mitchell, Kris Peach, Bill Edge (Chair), Professor Roger Simnett AO, Stein Helgeby

Absent: Judith Downes, Kevin Lewis

Role and composition of the FRC

01

FRC's role

The FRC is the peak body responsible for overseeing the effectiveness of the financial reporting framework in Australia.

Its key functions include: the oversight of the accounting and auditing standard setting processes for the public and private sectors; providing strategic advice in relation to the quality of audits conducted by Australian auditors; and advising the Minister on these and related matters to the extent that they affect the financial reporting framework in Australia.

The FRC monitors the development of international accounting and auditing standards, works to promote the development of a single set of accounting and auditing standards for worldwide use and promotes their adoption.

The FRC operates within a framework set out in Part 12 of the ASIC Act.

The ASIC Act sets out core objectives for accounting and auditing standard setting in Australia being that accounting and auditing standards should support the Australian economy by:

- reducing the cost of capital and enabling Australian entities to compete effectively overseas, and maintaining investor confidence in the Australian economy, including its capital markets; and
- being clearly stated and easy to understand.

“The FRC is the peak body responsible for overseeing the effectiveness of the financial reporting framework in Australia.”

The ASIC Act expressly limits the FRC's ability to become involved in the technical deliberations of the AASB and AUASB. In particular, it provides that the FRC does not have power to direct the boards in relation to the development, or making, of a particular standard, or to veto a standard formulated or recommended by the AASB or AUASB. This provision is designed to ensure the independence of the standard setting boards.

FRC members

Members of the FRC are appointed on a part-time basis by the Minister, typically for a term of three years.

The current membership of the FRC is as follows:



Mr Bill Edge Chair Financial Reporting Council

Bill is a retired partner of PricewaterhouseCoopers (PwC), having been a partner for 18 years. For his last eight years he led the PwC Australia Risk & Quality Group, which was responsible for risk management and quality control, including methodologies and technologies, across all of the firm's business units. He served on PwC's Global and Asian Risk & Quality Leadership Teams. He also spent six years leading the PwC Australian Professional Standards Group responsible for the firm's financial reporting and auditing policies and advice. He was also previously Chair of the Australian Auditing & Assurance Standards Board.

Bill was appointed Chair on 29 April 2016 and has been a member of the FRC since July 2014. His term expires on 28 July 2019.



Ms Jackie Callaway

Jackie was Group Financial Controller of Brambles Ltd from 2014 to 2017. Prior to this she was the Chief Financial Officer of privately-owned mining company Consolidated Minerals and, before that, worked for UK-listed Nikanor Plc. Jackie was also the Deputy Group Controller at leading New Zealand-based dairy producer, Fonterra, and started her career at two of the Big Four accounting firms, KPMG and Ernst & Young.

Jackie was appointed to the FRC on 29 April 2016 and her term expires on 28 April 2019.



Ms Judith Downes
Chair
Bank Australia

Judith is Chair of Bank Australia, the first customer owned bank in Australia. She has previously been a member of the Standards Advisory Council of the IASB and of the Australian Accounting Standards Board. She is an Honorary Fellow at the University of Melbourne. Judith's past experience includes Chief Financial Officer of a listed mining company, non-executive director of a listed property company, and Chief Financial Officer and Chief Operating Officer of the Institutional Division of one of Australia's largest banks.

Judith was appointed to the FRC on 29 April 2016 and her term expires on 28 April 2019.



Dr Stein Helgeby
Deputy Secretary
Department of Finance

Stein joined the Department of Finance in February 2010 as the Deputy Secretary of the former Financial Management Group. In October 2015 Stein was appointed Deputy Secretary of Governance and APS Transformation. Prior to this, Stein enjoyed a lengthy period in the Victorian Department of Treasury and Finance.

Stein was appointed to the FRC from 24 February 2010 to 23 February 2013, reappointed from 24 February 2013 to 23 February 2016, with an extension from 29 April 2016 to 28 April 2019.



Ms Noelle Kelleher
Chief Financial Officer
Vision Super

Noelle has nearly 30 years' experience in the financial services industry, with a particular focus on superannuation. Prior to joining Vision Super, Noelle was a partner at two of the Big Four professional services firms. Noelle is also company secretary for the Vision Super companies.

Noelle was appointed to the FRC on 3 June 2009 to 2 June 2012, reappointed from 31 August 2012 to 30 August 2015, with an extension from 29 April 2016 to 28 April 2019.



Mr Kevin Lewis
Chief Compliance Officer
Australian Securities Exchange

Kevin is the Chief Compliance Officer of the ASX and a member of the ASX Corporate Governance Council.

Prior to joining ASX, he was a lawyer for 30 years, specialising in financial services, mergers and acquisitions and corporate matters. He held a number of senior positions with law firms and as in-house counsel.

Kevin is also an Adjunct Professor with Sydney University Law School teaching financial services law.

Kevin was appointed to the FRC on 14 March 2011 to 13 March 2014, reappointed from 14 March 2014 to 3 April 2017, with an extension from 4 April 2017 to 3 April 2020.



Mr Graeme Mitchell
Chair
XRB

Graeme is a chartered accountant and professional director, being Deputy Chair of National Provident Fund Board of Trustees and a Director of Barnardos New Zealand and Retirement Income Group Limited. He also chairs the Audit Committees of the Ministry of Justice, the Ministry of Social Development, and the Human Rights Commission, and is an independent member of the audit committee of Porirua City Council. He is also the Honorary Consul General for Norway and was made an Officer of the Royal Norwegian Order of Merit in 2009 for services to Norway overseas.

Graeme is a retired Deloitte Audit and Assurance Partner.

Graeme was appointed to the FRC on 3 July 2014 and his term expires on 28 February 2019.



Mr David Nicol
Under Treasurer, Treasury and Economic
Development Directorate of the ACT Government

David, as Under Treasurer, advises the ACT Treasurer on the management of the Territory's budget, covering strategic issues of financial management, economic policy, revenue and tax policy and federal financial relations. David's responsibilities also cover matters of workers compensation, compulsory third party insurance and other insurances, and the shared corporate services provider for the ACT Public Service.

David is also Chair of the Heads of Treasuries Accounting and Reporting Advisory Committee and he has extensive experience in public budgeting and financial reporting and in public policy areas of social welfare and income support, government service delivery, industry, labour market and education.

David was appointed to the FRC on 3 July 2014 to 7 March 2017 and reappointed from 24 March 2017 to 23 March 2020.



Ms Kris Peach

Chair
AASB

Kris has extensive experience in accounting standard setting having previously served on the AASB as both a member and as the Deputy Chair and as a member of the Australian Urgent Issues Group.

Kris was previously a partner in KPMG's International Standards Group and Australia's Department of Professional Practice, interpreting complex technical accounting issues for a wide range of public and private entities. She also had a number of international financial reporting leadership roles within the firm.

Kris was appointed to the FRC on 3 November 2014 and her term expires on 2 November 2019.



Professor Roger Simnett AO

Chair
AUASB

Roger is also Scientia Professor of Auditing, UNSW Sydney where he has been head of the School of Accounting, Associate Dean Research of the Australian Business School and Academic Director of the Centre of Social Impact.

He has extensive experience in the auditing industry including significant involvement on international committees and advisory panels relating to auditing and assurance.

Previously he was a member of the IAASB and AUASB and is currently a member of the International Integrated Reporting Committee's framework review panel. Roger is a Fellow of the Academy of the Social Sciences in Australia.

Roger was appointed to the FRC on 1 April 2017 and his term expires on 31 March 2022.

Oversight of Australian standard setting

02

FRC functions

Under Part 12 of the ASIC Act the FRC's key functions include:

- Determining the broad strategic direction of the AASB and AUASB;
- Appointing members of the AASB and AUASB (other than the Chairs);
- Monitoring the operation of Australian accounting, auditing and assurance standards;
- Monitoring the development of international standards; and
- Giving advice or feedback to the Boards and their offices on priorities, business plans and procedures, budgets and staffing arrangements.

Determining strategic direction

Since its establishment, the FRC has made three determinations concerning the broad strategic direction of the AASB and AUASB:

- to require the AASB to work towards the adoption of accounting standards that are the same as those issued by the International Accounting Standards Board (IASB) (Direction approved 5 September 2002);
- to require the AASB to pursue the harmonisation of Government Financial Statistics (GFS) and Generally Accepted Accounting Principles (GAAP) reporting (Direction approved 12 December 2002); and
- to require the AUASB to use auditing standards issued by the International Auditing and Assurance Standards Board (IAASB) as a base from which to develop the Australian standards, to develop auditing and assurance standards other than for historical financial information, and to participate in audit research that is conducive to the AUASB's standard-setting activities. (Direction approved 4 April 2005).

Each of these directions is still current and the FRC continually monitors their appropriateness and is satisfied that the Boards have implemented these directions to the extent possible.

Appointment of members to the Boards

The FRC notes that both the AASB and AUASB have reduced the number of members over the past years to more appropriately reflect best practice, whilst still retaining an appropriate representation of skills and experience.

“Since its establishment, the FRC has made three determinations concerning the broad strategic direction of the AASB and AUASB.”

“The FRC notes that the 2016 results of the AASB review of IFRS adoption in Australia indicate that ... using IFRS as a base continues to be appropriate at this time.”

During 2016–17 the FRC approved the following appointments and reappointments to the Boards for the terms commencing in 2017:

AASB

- Ms Kimberley Crook (reappointment);
- Ms Regina Fikkers (reappointment);
- Ms Taryn Rulton (reappointment);
- Mr Marc Smit (reappointment); and
- Professor Stephen Taylor (appointment).

AUASB

- Ms Robin Low (reappointment);
- Mr Justin Reid (appointment); and
- Mr Gareth Bird (appointment).

The FRC was supported by the FRC Nominations Committee in this process.

The FRC acknowledges the contributions of retiring Board members:

AASB: Mr Peter Carlson, Ms Anna Crawford, Mr Steven Mitsas, Professor Ann Tarca.

AUASB: Ms Jane Meade and Ms Caithlin McCabe.

The ASIC Act provides that the members of the Boards (other than the Chairs) hold office on the terms and conditions determined by the FRC.

Monitoring the operation of Australian standards

The FRC monitors the operation of Australian accounting, auditing and assurance standards to assess their continued relevance and their effectiveness in achieving their objectives in respect of both the private and public sectors in the Australian economy. Based on the reports of the Chairs of the AASB and AUASB and the knowledge of the members of the FRC of how the standards operate in practice, the FRC is satisfied:

- the AASB and AUASB have incorporated IFRS and ISA Standards into Australian accounting and auditing standards within reasonable timeframes in accordance with the Strategic Directions;
- the AASB and AUASB have adequate post implementation review processes to assess the effectiveness of new standards and guidance and that regular agenda consultation processes identify existing accounting

and auditing standards where further guidance is necessary; and

- the AASB and AUASB appropriately consult before issuing new standards or guidance and that such mechanisms appropriately include roundtables, education sessions, webinars, podcasts, LinkedIn and Twitter.

The FRC notes that the 2016 results of the AASB review of IFRS adoption in Australia indicate that whilst further modifications to IFRS should be considered for specific issues in the not-for-profit sector, using IFRS as a base continues to be appropriate at this time.

The FRC also acknowledges and expects that the AASB performs this review from time to time.

Monitoring and influencing international standards

International accounting standards

In accordance with its governing legislation, the FRC seeks to support adoption of a single set of global financial reporting standards.

The international accounting standards with the most widespread acceptance are the International Financial Reporting Standards (IFRS) issued by the IASB. These have been adopted by over 100 countries, including China, European Union, India, Korea and New Zealand.

The FRC notes that the AASB monitors the work of the International Public Sector Accounting Standards Board (IPSASB) and where appropriate utilises their guidance to modify IFRS for the not-for-profit sector. The FRC and the AASB reassess regularly whether the Australian public sector should be using IPSAS or IFRS.

The FRC continues to advise the IFRS Trustees of its support for the IASB taking a more active role in setting standards for the not-for-profit private sector. The FRC supports the activities of the AASB in promoting more international consistency in reporting for the not-for-profit private sector.

International auditing and assurance standards

In accordance with its governing legislation, the FRC seeks to further the development of a single

set of auditing and assurance standards for world-wide use and promote international best practice in the Australian auditing and assurance standard setting processes. Consequently all AUASB pronouncements, where relevant, use the standards issued by the International Auditing and Assurance Standards Board (IAASB) as a base from which to develop the Australian auditing and assurance standards.

Additionally the AUASB regularly reports to the FRC its activities to build and enhance key relationships with both global and national standard setters designed to monitor and influence auditing and assurance developments.

International appointments

The FRC continues to monitor and influence the appointments of Australian representatives to key international bodies. Current Australian members on key international bodies include:

- IASB member — Professor Ann Tarca;
- IAASB member — Ms Fiona Campbell;
- IFRS Foundation Trustee — Ms Lynn Wood;

- IASB Accounting Standards Advisory Forum (ASAF) members — Ms Kris Peach, working with the NZASB representative, Ms Kimberley Crook;
- International Ethics Standards Board for Accountants (IESBA) member — Mr Ian McPhee; and
- International Public Sector Accounting Standards Board (IPSASB) member — Mr Mike Blake.

The FRC also acknowledges the significant contribution of Ms Merran Kelsall who, in addition to her role as Chair of the AUASB, was a valuable member of IAASB.

“The FRC continues to monitor and influence the appointments of Australian representatives to key international bodies.”

Giving advice or feedback to the Boards and their offices

FRC members participated in the inaugural joint strategy day for the AASB and AUASB and provided input to the development of the joint strategy and joint charter. In addition, the FRC provided input on the AASB's For-Profit Standard Setting Framework and the Not-for-profit Standard Setting Framework, which set out the way in which the AASB adopts IFRS, where appropriate, and modifies it for the not-for-profit sector. The FRC also provided input to the AASB's Review of IFRS Adoption in Australia.

The FRC provided feedback on the regular written and oral reports on the activities of the AASB and AUASB, in particular the Boards' reported progress against their respective strategies and corporate plans.

The FRC is satisfied that the advice or feedback provided

has been appropriately addressed by the AASB and AUASB.

The FRC considered the new Australian standards and guidance issued by the respective Boards in 2016-17 and was satisfied that due process had been undertaken.

Further details of the activities of the AASB and AUASB are provided in their annual reports.

Regional relationships

Australia and New Zealand continue to work closely together to facilitate harmonisation of Trans-Tasman standard setting.

In New Zealand the External Reporting Board's (XRB) structure contains three entities, the Board of the XRB and two standard setting boards – the New Zealand Accounting Standards Board (NZASB) and the New Zealand Auditing and Assurance Standards Board (NZAuASB).

The FRC Chair is a member of the XRB as part of the arrangement for cross-appointments between Australia and New Zealand.

The Chairs of the AASB /AUASB and the NZASB/NZAuASB are also each a member of their counterpart board.

The AASB and NZASB also work closely on the IASB's ASAF. The AASB also continues to closely work with the Asian Oceania Standard Setters Group (AOSSG).

The AUASB is an active member of the IAASB's National Standards Setters group where it works closely with the NZAuASB and other prominent auditing and assurance standard setters from the world's largest economies.

“Australia and New Zealand continue to work closely together to facilitate harmonisation of Trans-Tasman standard setting.”

Audit quality

03

Background

Australia has comprehensive legislative and professional requirements concerning audit with the main legislative requirements set out in the Corporations Act 2001 (Corporations Act). ASIC is the key regulator under the Corporations Act and has responsibility for the surveillance, investigation and enforcement of the financial reporting requirements of the Corporations Act, including the regulation of audit requirements.

The Corporations Act also gives legal effect to the auditing standards developed by the AUASB. The auditing standards require that auditors adhere to the relevant ethical standards as issued by the Accounting Professional and Ethical Standards Board (APESB). The professional accounting bodies enforce professional standards and comprise: Chartered Accountants Australia and New Zealand

(Chartered Accountants ANZ); CPA Australia; and the Institute of Public Accountants (IPA).

Under the ASIC Act, the FRC is to provide strategic policy advice and reports to the Minister and professional accounting bodies in relation to the quality of audits conducted by Australian auditors. This advice may include: matters relating to the effectiveness of Corporations Act provisions relevant to audit; the review processes undertaken by the professional bodies to ensure that auditor skills and processes remain at a high level; and disciplinary processes.

The FRC continued to actively monitor international developments in audit quality processes and assessed their potential impact on, and usefulness for, Australian practitioners and the financial reporting system.

“FRC is to provide strategic policy advice and reports to the Minister and professional accounting bodies in relation to the quality of audits conducted by Australian auditors.”

Stakeholder initiatives

Stakeholders, particularly ASIC and the professional accounting bodies, undertake a range of activities throughout the year with the objective of contributing to audit quality improvement.

Some notable initiatives during 2016-17:

- ASIC released three information sheets related to audit quality:
 - Information Sheet 222 *Improving and maintaining audit quality* – outlines considerations for auditors to improve and maintain audit quality;
 - Information Sheet 223 *Audit Quality: The role of others* – outlines how parties other than audit can contribute to audit quality; and
 - Information Sheet 224 *ASIC audit inspections* – outlines ASIC’s approach to inspecting audit firms and measuring inspection findings.
- Chartered Accountants ANZ:
 - Issued *Audit Essentials* guidance for 31 December 2016 and 30 June 2017 that included matters raised in the ASIC inspection process;
- Updated the *Audit Manual for Small and Medium Sized Entities* and the *Self Managed Superannuation Fund (SMSF) Audit Guide and Toolkit* to provide practical applications of quality control and documentation requirements; and
- Released a *Fraud Stories* series which features short clips of auditor members sharing their stories of encountering and addressing fraud situations in an audit.
- CPA Australia:
 - Sought to improve the quality of SMSF audits through bringing the CPA Quality Review Program team together with the ATO’s audit review team to identify common areas of concern in the audits of SMSFs, as well as publishing articles and podcasts to draw attention to identified compliance issues for SMSF auditors; and
 - Issued an updated *Small Entity Audit Manual* to assist auditors in auditing small entities.
- Institute of Public Accountants:
 - Held member workshops to discuss and address SMSF audit issues and areas of common concern; and
 - Reviewed SMSF audit checklists and material on ‘Who can audit what’.

Review processes

Australia’s auditor regulatory regime involves cooperation between ASIC and the professional accounting bodies. Each organisation runs an inspection or review program which encompasses audit engagements. Each of the programs is different and complementary to manage different risks, participants and types of engagement and to maintain a focus on audit quality. Accordingly, statistics gathered by each organisation may not be comparable.

ASIC Audit Inspection Program

ASIC inspects audit firms that audit listed entities and significant public interest entities. These are mostly large and medium size firms and are not subject to a duplicate review by the professional accounting bodies. All audit partners reviewed are Registered Company Auditors.

In June 2017, ASIC released the results of audit firm inspections for the 18 months to 31 December 2016. They are summarised in the table below:

	18 mths to 30 June 2015	18 mths to 31 December 2016
Audit firms reviewed	21	23
Audit files reviewed	111	93
Key audit areas reviewed	463	390
Key audit areas non-compliant ¹	19%	25%

¹Key audit areas non-compliant means that the auditor did not obtain reasonable assurance the financial report as a whole was free of material misstatement.

ASIC's findings are similar in nature to previous years and those of audit oversight regulators in other countries.

When releasing its report, ASIC said that auditors play a critical role in ensuring investors can be confident of the soundness of financial reports and well informed.

Given the efforts by firms to improve audit quality and the consistency of execution of audits, ASIC is of the opinion this is a disappointing result. ASIC believes the findings suggest that further work and, in some cases, new or revised strategies are needed to improve quality.

ASIC's findings do not necessarily mean that the financial reports audited were materially misstated. Rather, in ASIC's view, the auditor did not have a sufficient basis to support their opinion on

the financial report. ASIC's inspections focus on higher risk audit areas, and so caution is needed in generalising the results across the entire market. The results should be viewed as an indication of how some firms address more challenging audit situations.

ASIC said that audit firms should continue to pay particular attention to:

- *the audit of asset values* – particularly impairment of non-financial assets – including challenging the reasonableness of any forecasts and key assumptions, and the basis of valuation;
- *the audit of revenue* – including accounting policy choices, substantive analytical procedures, and tests of detail; and

- *maintaining a strong culture of audit quality* – including strong messages from firm leadership, setting expectations, leading by example, coaching, robust review processes, and effective accountability mechanisms.

ASIC also works with securities and audit regulators in other countries to promote audit quality.

Other ASIC activities to support audit quality include its financial reporting surveillance program, auditor surveillances not related to their inspections, investigations into corporate collapses, and addressing matters from complaints and other intelligence.

In 2016-17 ASIC:

- cancelled three registrations of company auditors following audit quality concerns; and
- removed 407 auditors who did not meet their obligations from the SMSF auditor register.

Chartered Accountants ANZ Quality Review Program

The Chartered Accountants ANZ Quality Review Program is designed to assess whether the approximately 11,300 Australian members (auditors and non-auditors) who hold a Certificate of Public Practice have implemented appropriate quality control policies and procedures in their practices.

The overall results of the Chartered Accountants ANZ Quality Review Program from the 222 firms (including audit firms, non-audit firms and mixed firms) reviewed in 2016-17 are summarised in the table below:

	2015-16	2016-17
Satisfactory	81%	83%
Re-review required in 12 months	19%	17%
Unsatisfactory	0%	0%

The majority of re-reviews were required as a result of inadequate quality control procedures or insufficient documentation of audit evidence, or a combination of both.

Chartered Accountants ANZ compiled a comprehensive list of top issues found during reviews of audit practices, and the related tools and resources available to assist members achieve compliance.

In terms of disciplinary processes, in 2016-17 Chartered Accountants ANZ considered 199 matters (arising from complaints against members, limited surveillance activities and internal compliance matters). Of these, 12 related to audit activities.

CPA Australia Quality Review Program

CPA Australia members who hold a Public Practice Certificate (approximately 6,700 members) are subject to the CPA Australia Quality Review Program. These reviews include members who are Registered Company Auditors.

CPA Australia expected, in the 2017 calendar year, to review over 1138 members in the Quality Review Program and to conduct a further 70 'follow up' reviews.

The results from CPA Australia Quality Review Program for the past two years are summarised in the table below:

	2016	2017
'Accept' reports – no departures identified	30.3%	26.6%
'Minor departure' reports – no serious departures identified	62.3%	62.1%
'Follow-up' reviews – multiple departures identified	7.4%	11.3%

The philosophy of the program is that compliance is based on good education. By continually sharing the outcomes and observations from the Quality Review Program, CPA Australia partners with members to focus on improving audit quality.

IPA Quality Review Program

The IPA requires all members who are issued with a Certificate of Public Practice (approximately 4,100) to undertake a Public Practice Quality Assurance Review every three to five years. All Registered Company Auditors are reviewed every three years.

In the last financial year, the IPA undertook a review of over 800 members in public practice and there was minor

non-compliance relating to CPD hours and producing documents relating to ATO lodgement.

Results of the IPA Quality Review Program were:

- 94 per cent of members met all professional standards and requirements or had minor non-compliance issues which were resolved before the review was finalised; and
- 6 per cent of members reviewed showed a level on non-compliance where follow-up action was required. All matters were resolved after follow-up action.

These results were similar to last year.

FRC overall view

The FRC notes the lack of improvement found by the ASIC Audit Inspection Review Program. The FRC will continue to work with ASIC, the AUASB, the accounting bodies and others to understand the root causes of non-compliance and remedial measures required. At this time, the FRC considers that it is premature to propose changes to the

Minister but will continue to monitor closely actions taken and results achieved over the next year. In particular, the FRC will encourage greater consistency and transparency of the respective quality review programs conducted by the accounting bodies.

“The FRC will continue to work with ASIC, the AUASB, the accounting bodies and others to understand the root causes of non-compliance and remedial measures required.”

Governance and administration

04

Attendance at meetings

FRC

The FRC held four meetings in 2016–17 in September, November, March and June.

Members' attendance at FRC meetings is shown in the table below:

Member	No. meetings attended/No. eligible to attend
B Edge (Chair)	4 of 4
J Callaway	4 of 4
J Downes	3 of 4
S Helgeby	4 of 4
N Kelleher	4 of 4
M Kelsall	3 of 3
K Lewis	4 of 4
D Nicol	3 of 4
K Peach	4 of 4
R Simnett	1 of 1
G Mitchell	3 of 4

FRC Nominations Committee

The FRC Nominations Committee held 5 meetings in 2016-17. Members of the FRC Nominations Committee as at 30 June 2017 are: Stein Helgeby (Chair), Bill Edge, Jackie Callaway, Judith Downes, Kris Peach and Professor Roger Simnett AO.

Members' attendance at FRC Nominations Committee meetings is shown in the table below:

Member	No. meetings attended/No. eligible to attend
S Helgeby (Chair)	5 of 5
B Edge	4 of 5
J Callaway	4 of 5
J Downes*	1 of 3
M Kelsall	3 of 4
K Peach	5 of 5
R Simnett	1 of 1

* Not eligible to attend two meetings due to a conflict of interest

Communication and consultation

The FRC uses its website (www.frc.gov.au) and meetings with stakeholders and other interest groups as its primary means of communication and consultation. An FRC communiqué of each FRC meeting is published on the website and distributed to key stakeholders. The website also includes information about FRC members, minutes of meetings, published reports and procedural rules.

Finances

In 2016-17, the Australian Government provided funding through the Treasury to support the FRC. The FRC's Secretariat is provided by staff of the Treasury's Markets Group. Expenditures and

performance of its functions are included in the Treasury's annual financial statements.

Funding of the AASB and AUASB (including the sources of that funding) is included in the annual reports of the AASB and AUASB.

Freedom of information

Since 1 May 2011, agencies subject to the Freedom of Information Act 1982 (FOI Act) have been required to publish information to the public as part of the Information Publication Scheme. This requirement is in Part II of the FOI Act and has replaced the former requirement to publish a section 8 statement in an annual report. All information published by the FRC can be accessed from links on the

home page of the FRC's website (www.frc.gov.au).

The FRC did not receive any applications for access to documents under the FOI Act during 2016-17.

Regulatory Impact Statements

The FRC did not submit any Regulatory Impact Statements in 2016-17.

"An FRC communiqué of each FRC meeting is published on the website and distributed to key stakeholders."

www.frc.gov.au