

Contractual arrangements for audit service providers

1.1
Appointment

1.2
Payment
procedures

1.3
Contracted
audits—frequently
asked questions

1.1 Appointment

1.1.1 Term of appointment

We usually appoint audit service providers for three years. We may extend this for up to a further two years if the provider meets performance requirements. All extensions are subject to evaluation and consultation.

1.1.2 Five-year rotation policy

We will not appoint an auditor to a particular audit for more than five years. However, after five years, we may decide to appoint another auditor from the same firm to the audit.

1.1.3 Ending a contract

We may terminate your contract if you are not carrying out your duties and functions in keeping with:

- the *Audit Act 1994*
- the terms and conditions of the contract
- our performance standards and guidance statements.

1.1.4 Conflict of interest

Within the public sector environment, our independent audit work fulfils the essential role of keeping Parliament and the public fully informed through our various reports and by providing an opinion on the published financial and other accountability statements of public entities.

Therefore, it is important that the independence of the external audit process not be called into question as a result of actual, perceived or potential conflicts of interest. Such conflicts could arise when you or a member of your firm carries out other services, including non-audit services, for the entity you are to audit.

To maintain the independence and objectivity of the audit process, you must avoid all situations that establish or have the potential to establish a conflict of interest or the appearance of a conflict of interest.

Public entities may ask you or your firm to provide accounting or consulting work—particularly with more commercialisation of government services—but you are not to carry out this work. However, you may carry out additional assurance work from time to time, if we approve it in advance.

You and other members of your firm are not to provide other services to the client during the period of your contract with us, unless we provide you with prior written approval.

In considering whether an actual or perceived conflict will arise, you must assess whether the other services you are to provide affect your independence. You need to take into account the Auditor-General's broader performance audit role.

Types of services that give rise to a conflict include:

- internal audit, asset valuation, taxation advice, and actuarial services
- accounting policy advice
- setting up, preparing and/or maintaining accounting records and systems.

Types of services that may give rise to a conflict include:

- preparing financial and other accountability statements
- services related to fundamental aspects of the client's business and/or strategic planning, including consultancy services.

Clause 10.2(b) of the contract requires you to inform us of any matter that might give rise to such a conflict of interest.

1.1.5 Quality assurance program

We require audits to be carried out in keeping with the:

- Auditing and Assurance Standards Board's auditing and assurance standards
- the Accounting Professional and Ethical Standards Board's professional and ethical standards.

This includes putting into effect quality assurance and engagement quality control review procedures required by APES 320 *Quality Control for Firms* and ASQC 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Reports and Other Financial Information, and Other Assurance Engagements*.

We expect you to have in place systems and processes to ensure that you comply with APES 320 and ASQC 1.

If we determine that an audit is of high risk, then we require you to appoint an engagement quality control reviewer to the audit.

In keeping with Auditing Standard ASA 220 *Quality Control for an Audit of a Financial Report and Other Historical Financial Information*, the engagement quality control reviewer must evaluate objectively the engagement team's significant judgements and the conclusions in the auditor's report. This evaluation will include:

- discussing significant matters with the engagement partner
- reviewing the financial reports and the proposed auditor's report
- reviewing selected audit documents relating to the significant judgements the engagement team made and the conclusions it reached
- evaluating the auditor's conclusions and considering whether the proposed auditor's report is appropriate.

In keeping with Australian auditing standards and the contract, your work will also be subject to our quality assurance program. This is detailed in **Section 4** of ASPI.

1.1.6 Financial Audit Tender Panel

We use private audit firms and experts, appointed by the Auditor-General under the provisions of the *Audit Act 1994*, as a core feature of our operations.

Our Financial Audit group is responsible for auditing financial reports on the public sector. We are committed to meeting good-practice standards in procuring these services and have adopted procurement practices that are in line with the Victorian Government Purchasing Board's guidelines.

We used to carry out an open public tender every year to appoint audit service providers for these services. This required considerable effort on our part and on the part of firms at a time when they are heavily involved in delivering existing audit demands.

In 2014, a review of the tender process determined that setting up a panel would benefit us and the firms that submit tenders as part of the process. The Victorian Government Purchasing Board recommends adopting a panel process if it is likely it to reduce costs and improve efficiencies for business and government. By identifying the 'best in market' participants, we can coordinate supply firms and reduce the inefficiencies of a too-rigorous approach through an open tender.

In 2015, the panel replaced the public tenders. The panel was set up for five years, with an option to extend the term of members by a further two years.

Every reporting period, we will ask firms on the panel to submit quotes for the financial audit of selected public entities. We do not guarantee that we will offer those firms contracts.

Having the panel allows us to:

- gain ready access to a pool of highly skilled contractors with the relevant experience and expertise to support the work of the Financial Audit group
- streamline and improve the process for seeking quotes and choosing suitable contractors
- reduce administrative costs
- allow members to submit quotes for specific engagements throughout the panel's contract period
- maximise value for money when engaging contractors.

If you have any questions about the Financial Audit Tender Panel process, email them to tenders@audit.vic.gov.au.

1.2 Payment procedures

1.2.1 General principles for paying contracted audit fees

We will pay your audit fees after receiving a valid tax invoice in line with our contract and key deliverables being achieved.

The contracted audit fee includes all your costs and expenses incurred in providing the audit services, including insurance costs, taxes, disbursements and imposts paid.

Within 30 days of you achieving each audit phase and the required key deliverable(s), you are to send us a valid tax invoice.

The four audit phases are:

- planning phase
- interim phase
- completing the audit and recommending the Auditor-General's opinion
- final phase.

You need to certify that you have successfully completed each of these four phases and submit a key audit deliverable as outlined in Appendix A.

We will pay the audit fee within 30 days of receiving a valid tax invoice if our Financial Audit Sector Director is reasonably satisfied that you have completed the audit phase and applicable key deliverables in keeping with the contract.

1.2.2 General rule for audits

After you complete each phase of the audit, we will pay you a proportion of the audit fee relating to that phase.

Where the contract audit fee is \$5 000 or more, we will pay the fee in instalments (unless the Assistant Auditor-General, Financial Audit otherwise approves it) as follows:

- 25 per cent when you complete the planning phase
- 25 per cent when you complete the interim phase
- 30 per cent when you complete the audit and recommendation of Auditor-General's opinion
- 20 per cent when you complete the final phase of the audit, when you have completed all deliverables to the required standard.

You must certify that you have completed each of these four phases and submit a key audit deliverable, as outlined in Appendix A.

1.2.3 Small audits—one visit

After you complete each phase, we will pay you a proportion of the audit fee relating to that phase.

Where the contract audit fee is less than \$5 000, we will pay you in instalments—unless otherwise approved by the Assistant Auditor-General, Financial Audit—as follows:

- 20 per cent when you complete the planning phase
- 0 per cent when you complete the interim phase
- 60 per cent when you complete the audit and recommendation of Auditor-General's opinion
- 20 per cent when you complete the final phase of the audit, with all deliverables completed to the required standard.

You need to certify that you have completed each of these four phases and submit a key audit deliverable, as outlined in **Appendix A**.

1.2.4 Additional audit fees

We will consider additional audit fees when you need to perform certain additional audit procedures because of:

- a request from us to carry out specific audit tasks that are not part of the normal audit tasks
- major breakdowns in internal controls requiring a substantial increase in substantive testing
- difficulties associated with forming an audit opinion on the financial statements due to the client's inability to prepare such statements in keeping with Australian Accounting Standards or any applicable reporting requirements
- further audit investigation arising from the detection of fraud
- significant change to the scope and nature of an entity's activities since the time the contract scope and fee was established
- the establishment of a new entity or segment of operations since the previous audit
- late changes in external regulations or policies which have a major impact on the completion of the audit of the financial statements.

Before carrying out any work that may give rise to an additional fee above the approved contract fee, you must:

- discuss with the sector director the need for additional work and obtain their written agreement about the reasons additional work is required
- write to the sector director, detailing:
 - the reasons for the additional work
 - your estimate of the number of extra hours required
 - your estimate of the additional fee to be requested
- direct additional audit fee requests to the responsible sector director.

We will tell you when we reach agreement with the client on the additional work proposed.

After the Assistant Auditor-General, Financial Audit approves the fee, the sector director will confirm the additional fee with the entity's chief executive (or other nominated officer).

In the final management letter, you must explain the circumstances that gave rise to the additional fee.

If you do additional work without our prior written approval, we reserve the right not to pay you for that additional work.

Audits of a new entity

Whenever you become aware of a new entity that may require an audit, you must inform the relevant sector director. The sector director, in consultation with the Assistant Auditor-General, Standards and Quality and the Assistant Auditor-General, Financial Audit will determine whether we have to audit the entity.

Under no circumstances is the audit of the new entity to proceed in your personal capacity or on our behalf, without our prior written agreement.

1.2.5 Invoice format

You must prepare a separate invoice for each audit client. You should set out each invoice as follows:

Name of client

Planning/interim/completion/final/additional* fee for the 201x/1y financial statement audit

\$xx xxx

GST \$x xxx

Total amount payable \$xx xxx

*delete whichever does not apply

Reconciliation:

Total contract fee \$xx xxx

Less: previously billed \$xx xxx

Less: this invoice \$xx xxx

Balance remaining \$xx xxx

You should invoice fees in line with contract schedules. We will not process invoices that amalgamate several contracted amounts into one fee amount and will return them to be rectified.

You should show additional fees separately.

1.3 Contracted audits—frequently asked questions

1.3.1 Carrying out extra testing

Question

The client has asked me to perform extra testing in my own name in areas that are not relevant to the external audit, or that only have an indirect relevance. Can I do this extra testing?

Answer

This is likely to be considered additional assurance or internal audit work which is outside the scope of our mandate under the *Audit Act 1994*. You cannot carry out such work under your contract because this would give rise to a conflict of interest and be contrary to our independence obligations.

1.3.2 Performing a review of half-year financial statements

Question

The client has asked me to review in my own name financial statements prepared halfway through the financial reporting period. Can I accept this work?

Answer

As the requested work is an assurance engagement which overlaps with our legislative responsibility—the period would subsequently be included in the audit of the financial year—you should do the work as part of the annual financial statement audit and not your own name. Ask the Assistant Auditor-General, Financial Audit for approval of this type of work before starting it.

1.3.3 Audit service provider firm merges

Question

On 1 July 201X, my firm will merge with a firm that has an employee who is an ongoing board member of a client. Can I perform the audit for that year?

Answer

No, not unless the employee resigns from the board position. You must not only be independent, but also be seen to be independent and avoid any potential or perceived impairment to objectivity. You must inform us immediately so that necessary arrangements can be made for the audit.

1.3.4 Quality assurance review by a professional body

Question

The Australian Securities and Investment Commission has decided to review the quality of an audit I am doing for someone else. Do I need to tell you?

Answer

Clause 3.5(g) of your contract requires you to inform us of the quality assurance review, including any adverse findings or penalties.

You should also tell us whether you are subject to any investigations by regulatory or professional bodies, so that appropriate action can be put in place to mitigate the risk to us, the audit or the Auditor-General's reputation.

1.3.5 Public relations strategy for the client

Question

My firm is intending to tender for a contract to develop a public relations strategy for a client. Is this acceptable?

Answer

This will depend on the facts and circumstances. You must discuss any such situation with us and we must agree to your tendering for the contract before you proceed.

1.3.6 Starting an audit in the last year of a five-year cycle

Question

I took over an audit in the last year of a five-year contract cycle for that entity. Does the five-year rotation policy disqualify me from tendering again for that audit?

Answer

You may tender for the audit only for a four-year period—three years with a one-year option—instead of the standard five years (three years plus a two-year option).

1.3.7 Ownership of audit work papers

Question

Who owns the working papers I generate and who has responsibility for their retention?

Answer

Audit files relating to audit work you carry out, including all written or electronic audit working papers, remain our property. While you are appointed, you will hold the audit files on our behalf and will give them to us on request in a readable form and reasonable time frame. During an audit, files relating to the current audit must always be available to us.

When the contract period ends, you are to retain all working papers on our behalf and make them available to us on request. Where the audit contract is awarded to someone else, we may ask you to give the audit working papers to the new service provider. All working papers, as defined by the Public Record Office Victoria, are temporary records and must be retained for at least seven years after the audit is completed. They may then be destroyed securely.

You must take all reasonable steps to maintain the security of all audit files from unauthorised access, release, damage, alteration and malicious tampering.

1.3.8 Providing audit services outside Australia

Question

Can I do some audit work overseas?

Answer

Unless we have given you prior written consent, under your contract agreement, you must not hire anyone outside Australia to provide any or part of the audit services to:

- the Auditor-General
- the public entity
- yourself.