Stakeholders want fraud detectors, says Lucy

Stakeholders have increasing expectations that auditors will detect fraud as a part of the work they do when undertaking the external audit of a company, according to Jeff Lucy, the acting chairman of the Australian Securities and Investments Commission (ASIC).

Lucy told a business forum hosted by the Institute of Chartered Accountants held in Queensland in the past week that the old adage of auditors needing to be ‘watchdogs’ rather than ‘bloodhounds’ is being turned on its head by a market demanding more from the providers of the external audit services.

‘You will be aware of the view expressed in some quarters that in fact auditors ought not be just “watchdogs”, but in fact should be closer to “bloodhounds” — a term which clearly calls for greater vigilance and an even more robust attitude to the job at hand and the entity being audited,’ Lucy says.

“I would say that there is, in fact, now a clear market expectation to this effect — that is, that auditors are bloodhounds not just watchdogs. Simply put, the market expects auditors to pick up instances of fraud. It expects auditors to take the initiative where they discern something amiss — to find and reveal what is hidden. That expectation has, if anything, increased over recent years.’

He says the auditor is a class of professional that has always been wedged between two sets responsibilities that can sometimes conflict. ‘Auditors in particular have always faced the dilemma of trying to reconcile a commercial service provider–client relationship with the responsibility of a watchdog or a “contracted regulator” of corporate financial reporting,’ the acting ASIC chairman says.

Lucy says the reforms contained in the ninth tranche of the Corporate Law Economic Reform Program (CLERP) tries to address this to some degree despite the fact parts of the legislation are not in line with overseas precedents. He says amendments proposed to the existing Bill currently before Parliament by the Federal Opposition, particularly regarding prohibitions on the provision of certain non-audit services by the external auditor, would bring Australia into line with the United States and Canada.

‘That is, the US already conditionally prohibits services such as: bookkeeping services related to the accounting or financial statements of the audit client, financial information systems design and implementation, appraisal or valuation services, fairness opinions, actuarial services and internal audit outsourcing services by the auditor,’ says Lucy, a former chairman of the Financial Reporting Council.

Proposed opposition amendments to the CLERP 9 legislation, which is expected to be in force by 1 July 2004, also affect the cooling-off period. The general feeling from within the accounting profession is that a two-year cooling-off period is adequate, but the Federal Opposition is pursuing the instatement in legislation that a four-year cooling-off period be enshrined in law.

A four-year cooling-off period would mean an auditor could retire from an accounting firm but would be prohibited from joining the board of a former audit client for a four-year period.

This suggested amendment has its origins in the report of the Royal Commission into the collapse of the general insurer HIH.

The amendments proposed by Labor, Lucy explains, may be an attempt by the Federal Opposition to strengthen the laws that are now expected by stakeholders to be somewhat tough.

'It may also acknowledge the reality that in a dynamic and fast-moving international marketplace, Australia simply cannot afford to lag behind in any way, and that this is an opportunity for the Parliament to ensure that our laws are truly internationally credible and can respond to the high expectations about regulation that investors and consumers now have,' Lucy says.

This article was supplied by Tom Ravlic. Tom Ravlic is a financial journalist who has spent the past seven years covering the accounting profession, accounting and audit standard setting and corporate governance. His work has appeared in various publications including *Business Review Weekly*, *Personal Investment* (now *Personal Investor*), *The Age*, *CFO Magazine*, the *Australian CPA*, the *Company Director Journal* and the newsletters of the internationally renowned Lafferty Group. In addition to his freelance commitment to a wide range of publications, Tom has recently accepted an appointment to be editor of *Chartac Accountancy News*, published by Melbourne-based publisher Crown Content.