



JUNE 2022

Auditor Regulation and Oversight Plan 2022-2025

This document is for:

- Registered auditors
- Accredited bodies
- People who prepare financial statements for FMC reporting entities
- Directors of FMC reporting entities

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Contents

Executive summary	3
Our role	3
Our focus	4
The purpose of auditor regulation	7
Improving investor confidence	7
Recognition of New Zealand auditors overseas	7
Improving audit quality	9
How we review audit quality	9
Key audit areas	12
Education and communication	13
The role of accredited bodies	13
Appendix: Regulatory responsibilities	16

Executive summary

Our role

The main statutory objective of the Financial Markets Authority - Te Mana Tātai Hokohoko is to promote and facilitate the development of fair, efficient and transparent financial markets.

Improving audit quality and maintaining international standards and recognition for auditors are key to promoting trust and confidence in New Zealand's capital markets and supporting our overall objective.

Audited financial statements are an important resource for investors when making investment decisions. Investors' confidence in financial statements is dependent on the perceived quality of the audit. Auditor regulation and oversight helps ensure the businesses we regulate (known as Financial Market Conduct (FMC) reporting entities) have access to competent auditors, and that these audits (known as FMC audits) are of a high standard. To achieve this we:

- review the systems, policies and procedures that audit firms have in place to deliver high-quality audits
- review individual audit engagements, to ensure they meet the auditing and assurance standards
- monitor accredited bodies to ensure they are effective frontline regulators of FMC licensed auditors.

Our work in the direct audit oversight of licensed auditors and registered audit firms is separate from our monitoring of accredited bodies' functions – these roles performed by our Audit team and Market Infrastructure team, respectively.

To obtain and maintain recognition of New Zealand auditors in overseas jurisdictions we are required to meet international audit oversight standards in various jurisdictions. The FMA is a member of international oversight body IFIAR (the International Forum of Independent Audit Regulators), which allows us to maintain best practices, and contribute to and access relevant international knowledge and resources.

This document summarises our plan relating to auditor oversight, as part of our obligation under section 52 of the Auditor Regulation Act 2011 (the Act).

Our focus

We set out our focus areas at the start of each three-year audit cycle¹. Over the three years to 30 June 2025, we will focus on the following areas:



Improve audit quality by performing audit quality reviews at least every 3 years



Ensure auditing and accounting standards are being upheld



Thematic reviews may supplement our audit quality reviews



Monitor accredited bodies to assess their regulatory performance



Engage with stakeholder and oversea regulators to assess our audit oversight regime

Improve audit quality

We aim to perform audit quality reviews (AQR) every two years for the Big 4 audit firms² and at least once every three years for the other registered audit firms. We will ensure our key stakeholders, including audit firms, are informed about developments in areas impacting audit quality, and highlight the processes where improvements can be made.

Our AQRs are risk-based, and we consider various factors when determining which files will be reviewed and the areas that may require our specific focus. Accordingly, we may change our audit quality review schedule, perform unscheduled reviews of audit firms, and select audit files and identify key audit areas for our reviews based on specific risk factors.

¹ We are currently in year one of the three-year cycle.

² The four largest audit firms are Deloitte, EY, KPMG, and PwC.

Although our approach is aligned with international standards, we recognise that the financial markets are an ever-changing landscape. Auditors and audit firms are constantly evolving to ensure they keep up with new developments and requirements

The FMA is conscious that as the regulator we also need to evolve and keep pace with changes in the market. We will continue to look for ways where we can improve our processes and perform our duties more efficiently to remain a relevant regulator.

Ensure auditing and accounting standards are being upheld

As part of our AQRs, we will continue to focus on enhanced auditor reporting, assessing whether the auditor's report is a true and fair representation of the risks identified and work performed by the auditor. We will conduct a 'deeper dive' into the auditor's application of the standards and whether the auditor complies with the standards. We will also continue to focus on the practical implementation of the latest International Financial Reporting Standards (IFRS) and monitor the effectiveness of financial reporting.

As part of our stakeholder engagement, we will share our observations with the External Reporting Board (XRB) so they are provided with the necessary information to assess if any clarifications or changes to standards are needed.

Thematic reviews

During the 2023/2024 year, we plan to perform specific reviews of all audit firms' implementation of the new quality management standards. These standards³, effective in December 2022, are equivalent to the International Standards on Quality Management. The new requirements are more onerous than current requirements and increase the accountability of management at audit firms. We recommend that audit firms create robust plans to address these new requirements now, and not wait until the implementation date.

During the reviews, we will:

- assess how each audit firm has implemented the new standards
- assess whether the audit firm's system of quality management is appropriate
- review whether the audit firms complied with the standards during the first year that the standards were effective.

We will also aim to issue a separate report summarising our findings from these reviews. For subsequent review cycles, quality management systems will become part of the overall audit quality reviews.

We may also supplement our routine AQR with other thematic reviews on particular aspects of audit practices across audit firms, industries or sectors. Thematic reviews may be chosen to focus on an aspect of audit in greater depth than is generally possible in our AQR and may be dependent on the current economic landscape or common issues we observe in the market. This could involve adjusting our routine AQR to integrate thematic work. We may also release thematic review findings as separate reports, or as part of our annual audit quality report.

³ PES 3: Quality Management for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance or Related Services Engagements; PES 4: Engagement Quality Reviews; and ISA (NZ) 220 (Revised): Quality Control for an Audit of Financial Statements

Monitor accredited bodies

Part of the FMA's strategic priority to promote trust and confidence in capital markets is ensuring that frontline regulators are effective in their roles. We will continue to fulfil our requirement prescribed by the Act to monitor the accredited bodies – the New Zealand Institute of Chartered Accountants (NZICA)⁴, and CPA Australia – and ensure the audit regulatory systems and processes used by accredited bodies are adequate and effective.

Engagement with stakeholders and overseas regulators

We will continue to engage with relevant stakeholders and overseas regulators to share our findings and research, while also assessing if changes to our audit oversight regime are required to meet our objectives. Our involvement includes, but is not limited to:

- quarterly meetings with the local audit firms on audit and financial reporting matters
- attendance and participation at events hosted by IFIAR and accredited bodies
- presentations on audit quality at audit firms and universities, to share details of the work we perform
- continual discussions with the Ministry of Business, Innovation & Employment, the External Reporting Board (XRB), the Australian Security and Investment Committee (ASIC), and IFIAR and its members.

Climate-related risks in an audit of financial statements

Climate change is receiving increased attention from governments, investors, and other stakeholders, as climate change effects become more visible. In 2021, New Zealand introduced the Financial Sector (Climate-related Disclosures and Other Matters) Amendment Bill, requiring approximately 200 FMC reporting entities to provide separate disclosures on climate risk and the entity's emissions. This will be a requirement from financial years commencing in 2023.

Because climate change and associated risks, including physical and transitional risks, could impact the financial outlook and financial statements of FMC reporting entities, this affects the auditing of these entities.

We will inform preparers of financial statements, auditors, investors, and other stakeholders about our expectations for disclosures and accounting related to climate change. Within the next three years we expect our monitoring of audit files will include consideration of climate risks where they impact financial statements.

⁴ NZICA amalgamated with the Institute of Chartered Accountants in Australia (ICAA) on 1 January 2015, to form the Chartered Accountants Australia and New Zealand. However, for the purposes of the audit oversight regime, NZICA continues to be the accredited body.

The purpose of auditor regulation

One of the FMA's statutory functions is to promote the confident and informed participation of businesses, investors, and consumers in the financial markets. Confident and informed participation depends on investors and other stakeholders having access to credible and reliable financial information. Audits of FMC reporting entities' financial statements ensure their statements comply with financial reporting standards and give a true and fair view of the financial position of the entity.

Auditor regulation supports the quality and integrity of audits of FMC reporting entities. By ensuring a high standard of auditing, we aim to:

- increase investor confidence in the quality of the audited financial statements of FMC reporting entities
- give wider recognition to the professional status of New Zealand auditors in overseas jurisdictions.

Improving investor confidence

The Auditor Regulation Act 2011 regulates auditors' performance of financial statement audits of FMC reporting entities. The Act recognises this is a specialist job that cannot necessarily be performed by every qualified accountant.

Our 2019 report [Perceptions of Audit Quality in New Zealand](#) found reasonable levels of confidence in audit quality, but also a serious gap between the expectations of investors, and what auditors are delivering.

This report provides a baseline measure of confidence, trust, professionalism and perceived quality of the audit process, and the perceived benefits from the user's perspective. The findings and insights can help auditors and audit firms improve how they provide assurance to investors. Investors rely on audited financial information to support informed investment decisions, so it is critical for auditors to respond to investors' expectations.

We will continue to engage with relevant stakeholders to assess what changes can be made to better inform investors about audit quality.

Recognition of New Zealand auditors overseas

Another objective of the Act is to enhance the international recognition of New Zealand auditors. This is important as it gives overseas investors confidence that New Zealand's capital markets are subject to levels of oversight similar to other countries' capital markets.

We have received recognition from the European Union (EU) and Switzerland. This means New Zealand auditors can audit the financial statements of businesses listed in the EU and Switzerland. The recognition also confirms New Zealand's regulatory structure is robust and gives investors' confidence that New Zealand auditors meet international standards. We will continue to pursue further recognition where opportunities arise.

FMA's membership of IFIAR gives us access to international knowledge on auditor regulation. It also gives us greater opportunity to engage with the six largest international audit firms⁵. IFIAR's Multilateral Memorandum of Understanding (MMOU) contributes to the effective regulation of audit firms by improving information exchange and cooperation among members.

We are actively involved in IFIAR through the Emerging Regulators Group (ERG) and other taskforces. The ERG's purpose is to provide a meaningful platform for new and emerging audit regulators to exchange ideas and build capacity. As the current chair of this group, the FMA has the opportunity to share insights, improve our audit oversight, and achieve our objectives to maintain and increase international recognition. Our membership also gives us access to training and allows us to discuss and learn from the experiences and methodologies of other regulators. We are actively engaged in increasing our cooperation with other regulators.

⁵ The six largest audit firms are BDO, Deloitte, EY, Grant Thornton, KPMG, and PwC.

Improving audit quality

We aim to improve audit quality by reviewing audit files for compliance with the auditing and assurance standards. During each review of an audit firm, we explain the areas where the auditor did not comply with the standards, so the firm understands any issues identified and can improve these areas across their entire audit portfolio.

How we review audit quality

The Act requires us to perform an audit quality review of each registered audit firm at least once every four years. However, our aim is to keep our review cycle consistent with the EU's three-year cycle. The frequency of our reviews varies, depending on the size of the firm. We inspect the Big 4 audit firms every two years, while other audit firms are generally inspected every three years.

We review the quality systems, policies and procedures of audit firms against the requirements of the Act and the auditing and assurance standards. Audit firms must also use reasonable care, diligence, and skill in their FMC audits – we test this by reviewing a reasonable sample of individual audit files.

The reviews are carried out by FMA staff and contractors; where required, staff from overseas audit oversight bodies are seconded to the FMA. We also have an independent reviewer/observer involved in each review, to ensure the process is fair and equitable, and also to review our reports.

Thematic reviews will follow a similar process as the routine audit quality reviews, with a focus on the objective of the thematic review.

Our routine AQR process is outlined below.

Planning

Every year we produce a schedule of audit firms to review, in line with our review cycle. We communicate with the audit firms that will be reviewed and agree on suitable review dates.

Closer to the review date, we select files to inspect based on the following risk assessment factors:

- The risk the audited entity poses to investors. These entities may include listed companies, financial institutions, and large investment schemes.
- Engagement partners with previous non-compliance records or not previously reviewed.
- Entities that frequently change audit firms.
- Entities where we have previously noted issues with non-compliance.
- Other factors, such as the size of the entity and the audit fees in relation to substantial fees the firm may have received for non-audit work.

We also try to incorporate an element of unpredictability into our reviews.

The number of files selected per audit firm depends on the number of FMC audits and the number of audit partners in the firm, to provide sufficient coverage of the firm's work.

Quality reviews

The framework for our quality reviews is risk-based and includes an ongoing assessment of the audit firms, licensed auditors, and FMC audits. It provides the basis for planning the appropriate level and timing of interaction with each audit firm and licensed auditor, which is necessary to evaluate risk in each phase and target appropriate intervention to reduce risk to an appropriate level.

A team of reviewers performs the quality review in line with the minimum requirements of Section 68 of the Act. The quality review framework provides consistency in performing our reviews and ensures that each review meets the statutory requirements under the Act.

Audit files are evaluated for compliance with the auditing and assurance standards.

Any findings of each individual file are discussed with the relevant engagement partner of the audit. When necessary, the audit team provides further evidence and explanations.

Key audit areas

During our AQR, we will focus on key audit areas. The key audit areas are chosen based on common findings identified by international audit regulators and our own findings from recent reviews⁶. Our reviews for the next three years will focus on the key audit areas described on page 12.

Reporting

During our review we discuss the findings with the relevant engagement partner. We provide the audit firm with a draft report of our key findings related to the quality systems, policies and procedures of the audit firm, and review of the individual audit files. The report is reviewed by our independent reviewer before the audit firm has the opportunity to comment and provide us with further evidence about how they complied with the auditing and assurance standards.

In responding to the findings, the audit firm may include any improvements to their systems, policies and procedures, or any other specified actions which they consider will address the findings. Where the audit firm disagrees with a finding, we expect the firm to provide a detailed explanation together with copies of relevant documentation and confirmation of whether the documentation was made available to us or included in the audit file at the time of the review.

After considering the audit firm's comments, we prepare a final draft of the quality review report, which is provided to our Auditor Oversight Committee (AOC). The AOC provides independent advice to the FMA to ensure consistency and fairness between all quality reviews performed. The committee is made up of a diverse group of professionals, including ex-auditors, partners, company directors, and others with relevant experience.

Our final audit quality review report will include any recommendations we may have to improve audit quality, and conclude on the final ratings for the firm.

We also send entities whose audit files have been reviewed a letter to inform them of the review. We do not share the outcome of our reviews with the entities directly, but rather provide them with information to have a meaningful discussion about the quality of their audit and the audit firm more generally.

⁶ See our [Audit Quality Review Report 2021](#).

Next steps

We require the audit firm to prepare a remediation plan and a root cause analysis of the findings outlined in the report. We assess the appropriateness of the plan to ensure it is sufficient to address our findings. If we are not comfortable with the audit firm's plan, we may provide further guidance or issue directions.

Subsequent reviews of the audit firm and individual audit files help us assess the overall effectiveness of the root-cause assessment and the remediation activity that was carried out.

Where we do not see satisfactory results from an audit quality review, we will perform additional reviews outside of our normal review cycle.

In instances of significant breaches of the auditing and assurance standards, the matters may be referred to the relevant accredited body to further investigate the licensed auditor.

Key audit areas

Audit firm's system of quality management				
- Overall governance of the audit firm and the culture modelled by its leadership - The audit firm's internal and external audit quality reviews - How audit quality is considered in the performance assessment of staff and leaders - How the audit firm conducts root cause analysis when assessing the underlying cause of audit quality findings - The audit firm's plans to address findings from internal and external reviews, and how it monitors effective implementation				
Planning of the audit	Auditor independence - Effectively identify and assess any threats to their independence and apply appropriate safeguards - Report these properly to audit committees and directors - Appropriate disclosure and reporting of any significant non-audit services		Understand the entity and its environment - Properly identified the risks and documented key systems and processes - Assessed the controls that are relevant to the audit, and evaluated the design and implementation of those controls - Appropriately tested reliance that has been placed on controls - Assessed the impact of the controls' deficiencies on the audit work	
Execution of the audit	Execution of audit procedures - Documentation of audit procedures and results - Compliance with the audit firm's methodology and auditing standards		Audit evidence on the audit file Appropriate and sufficient audit evidence to support their opinion and to enable an experienced auditor, having no previous connection with the audit, to understand audit procedures and conclusions reached	
Reporting of the audit	Key audit matters - Whether the key audit matters were appropriately identified - Whether the audit work to establish key audit matters is appropriate - Whether the quality of information in the audit report provides relevant and meaningful information		Communication to those charged with governance (TCWG) - Evidence of discussions with and enquiries of TCWG - Appropriate reporting of significant matters, issues and deficiencies	
Significant matters	Professional judgement Sufficient audit evidence to demonstrate that the auditor's professional scepticism and judgement has been applied when assessing management's key judgements and assumptions	Significant risk areas - Understanding the entity's policies, processes, and procedures to identify significant balances and transactions - Performing tests that address the relevant assertions - Reassessing the audit approach when circumstances arise - Reporting issues and deficiencies to those charged with governance	Auditor responsibilities relating to fraud - Assessment of the risk of fraud, including fraud in revenue recognition and management override - Assessment of significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual - The auditor's requirement to test journal entries to supporting documentation	Audit fees - Impact of audit fee pressure on the quality of FMC audits - Initiatives to ensure audit quality is maintained

Education and communication

Our audit quality reviews determine the key messages and areas for improvement that will be the focus of our market engagement. We will ensure our key stakeholders, including audit firms, are aware of current issues with audit quality, and are kept up to date on key developments.

Many stakeholders play a role in improving the quality of FMC audits. Our communication about the audit oversight regime is designed to help these stakeholders contribute to higher-quality audits in New Zealand.

Over the next three years, this communication may include the following:

- This auditor oversight plan, which sets out the focus areas for our monitoring. The Act requires us to update this plan annually on a rolling three-year basis.
- Quality review assessment reports for audit firms after an audit quality review. These reports contain the findings of reviews and our recommendations for remediation.
- Presentations at audit firms to discuss what we found during their individual audit quality review, and how to improve their overall audit quality.
- Presentations or reports addressed to other stakeholders about the audit oversight regime, and how other businesses and professionals can contribute to audit quality.
- Ongoing dialogue with accredited bodies about our audit quality review findings and other trends in the audit industry. The aim is to improve the joint monitoring of licensed auditors, and address education issues.
- Thematic reports on audit quality matters, such as the key audit matters report.
- Annual reports of audit quality reviews, which summarise the findings for the year. These reports include recommendations for auditors and other stakeholders on how to improve audit quality. This enables auditors to willingly comply with our expectations, and the standards and legislative requirements.
- Letters to directors and audit committees about the quality of information provided to audit firms, or other non-compliance with accounting standards identified during our audit quality reviews.
- Collaboration with the External Reporting Board (XRB) to find areas for improvement, which XRB can use to influence international accounting standards, where needed.

Additionally, the [Perceptions of Audit Quality](#) survey highlighted the need to educate investors on the role of auditors. We will look for opportunities to communicate with investors about the nature of audited information, the oversight regime, and the role of the FMA.

The role of accredited bodies

While we carry out some areas of the auditor oversight regime directly, accredited bodies also have important responsibilities as frontline regulators. In accordance with the Act, the FMA monitors and reports on the adequacy and effectiveness of the accredited bodies' audit regulatory systems. An overview of the responsibilities of the FMA and the accredited bodies is set out in the Appendix.

Accreditation

Accredited bodies need appropriate systems, policies, and procedures in place to perform their audit regulatory functions. The accreditation process evaluates the systems, and how the entity will meet and maintain minimum standards of accreditation set by the FMA.

There are currently two accredited bodies in New Zealand, the New Zealand Institute of Chartered Accountants (NZICA), and CPA Australia (CPA).

How we monitor accredited bodies

In accordance with the Act, the FMA monitors the audit regulatory systems of the accredited bodies and must publish a report annually on the extent to which the audit regulatory systems are adequate and effective.

Our annual monitoring process includes regular communication and updates from the accredited bodies on the status of ongoing regulatory action, reports and notifications regarding licensed auditors. We expect accredited bodies to use their full range of regulatory tools and will work closely with them to coordinate these tasks, to ensure there are no gaps or possible duplication of work, and that appropriate action is taken when an issue is identified.

Each year, accredited bodies are also required to provide to the FMA a self-assessment of how they operate and monitor their own systems.

For each accredited body, we undertake a desk-based review of this information, select and review a sample of activities across all regulatory functions, and carry out an onsite visit. Following the review, we discuss our observations and findings, alongside any recommendations we intend to make to improve or remediate any matters identified. We have the power to direct an accredited body to amend its systems and processes where necessary.

The table below sets out the accredited bodies' regulatory functions, how they work, and how we monitor them to ensure they are effective.

Regulatory function	How the function works	How we monitor accredited bodies
Licensing domestic auditors and registering domestic audit firms	The FMA issues the prescribed minimum standards that audit firms have to meet. Accredited bodies have to notify us about licensing and registration approvals and failures.	We review a sample of licences and registrations assessed by accredited bodies to confirm whether the applicants have met the minimum standards. We also review any licences cancelled during the period.
Monitoring licensed auditors and registered audit firms	The Act requires accredited bodies to have adequate and effective systems to regulate auditors. We can request information about their monitoring at any time.	We review the policies and procedures in place to monitor and regulate licensed auditors, as well as specific monitoring that has taken place during the period in response to issues identified at a particular firm.
Promoting and monitoring competence	Licensed auditors must comply with the minimum standards the FMA sets for professional development and ongoing competence. There are also ongoing certified professional development (CPD) requirements set by the accredited bodies.	We review the availability of training provided by accredited bodies, and how they monitor compliance with ongoing professional development requirements. We select a sample of trainings, as well as monitoring reviews undertaken by the accredited bodies of auditor's CPD requirements.
Taking action against misconduct	Accredited bodies must report any complaints received about licensed auditors or registered audit firms to the FMA. We also have the power to start or take over investigations of misconduct and to take direct disciplinary action.	The FMA reviews accredited bodies' policies and procedures for dealing with misconduct of licensed auditors or registered audit firms. We also review any complaints about a licensed auditor to see if accredited bodies' policies and procedures were followed.

Appendix: Regulatory responsibilities

The table below gives an overview of the most significant auditor regulation activities set out in the Auditor Regulation Act 2011 and describes the role of the FMA and the accredited bodies in each activity.

Activity	What accredited bodies do	What the FMA does
Licensing of auditors and registration of audit firms	Licensing of domestic auditors and registration of audit firms, based on the prescribed minimum standards set by us.	Licensing of overseas auditors and audit firms based on the minimum standards prescribed by us, or on the basis of the Trans-Tasman Mutual Recognition Agreement.
Monitoring of licensed auditors and registered audit firms	Must have systems in place for ongoing monitoring of licensed auditors. Share reports, notifications, and intelligence with the FMA.	Conduct audit quality reviews (AQR) of registered domestic audit firms. We also assess the quality control systems at audit firms and review individual audit files. We perform other monitoring work following financial statement reviews, complaints, and referrals. We refer any complaints about FMC audits to the accredited body of the licensed auditor.
Promoting and monitoring the competence of auditors	Set CPD requirements and provide appropriate training for licensed auditors, and ensure they continue to meet the ongoing competence requirements.	Provide information to licensed auditors, registered audit firms, accredited bodies, FMC reporting entities and other stakeholders about the regulatory regime. After our quality reviews, we also share details of our findings and recommendations on how audit quality can be improved.
Investigations	Investigate any complaints about FMC audits from the public or the FMA. Must also follow up on complaints referred by us. In both instances, follow policies and procedures to ensure appropriate enquiries are made to determine if misconduct has occurred, and make referrals for disciplinary action to be considered.	To the extent determined appropriate and necessary, follow up on any referrals or any involvement with enquiries and investigations. If the accredited body decides not to investigate or does not investigate promptly, we may take over the investigation.
Taking action against misconduct	Follow its policies and procedures for taking disciplinary action, to achieve appropriate and proportionate outcomes where misconduct has occurred.	If we identify actual or potential misconduct through our AQR or other monitoring, we make a complaint to the accredited body of that particular licensed auditor and audit firm. The FMA can investigate only those matters that accredited bodies have referred to us or have decided not to investigate. We may also issue directions to licensed auditors and registered audit firms.

