

Working paper summary

Understanding Assurance in the Australian Self-Managed Superannuation Fund Industry

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Key Concepts/Themes

Pension funds; audit fees; industry specialisation; professional affiliations; auditor independence; non-audit services; Cooper Review;

Self-managed superannuation funds (SMSFs) represent the fastest growing and largest segment of the Australian retirement savings industry.

In 2010, the Federal Government commissioned the Super System Review into the governance, efficiency, structure and operation of the superannuation system. This inquiry, widely referred to as the Cooper Review, highlights a lack of basic knowledge and understanding of the SMSF segment and its auditors.

This study, which has been co-funded by the Centre for International Finance and Regulation (CIFR), examines audit and assurance issues in the SMSF sector including:

- Audit pricing;
- Audit partner specialisation;
- Non audit services and auditor independence;
- Auditor professional affiliations.

The study spanned the period from 2008 to 2010, and utilizes a sample of nearly 100,000 SMSFs.

The study addresses several key research issues, the first of which is whether SMSFs are charged premium audit fees. Related to this is the question of whether there is a correlation between the perceived quality of the audit and the fee charged. Another issue is whether the joint supply of non-audit services impacts audit independence.

In terms of audit pricing implications, the study considers whether partners having greater client numbers charge higher prices due to specialisation or take advantage of scale benefits to pass on fee discounts.

The audit pricing implications in the SMSF setting are interesting, given that the traditional agency cost issues associated with publicly listed companies are not present. This is because the owners of SMSFs are effectively the managers. It follows that price considerations will typically prevail over quality considerations, as a SMSF trustee is incentivised to place a greater emphasis on cost savings than on the auditor's reputation.

In an environment characterised by the absence of agency costs, and where demand-side incentives for superior quality auditing are low, the study finds that significant fee discounts are passed on by specialist partners auditing more clients. Interestingly, audit partners appear to be applying a service bundling strategy where scale benefits are applied to reduce audit costs with a view to growing their higher-margin non-audit services businesses. Fee premiums are observed to leading partners when total fees or a service bundle is considered.

A further fee-related finding is whether registered company auditors and members of similar professional bodies can command fee premiums for the perceived superior quality of their services. The study finds that, compared to audit bodies who do not enforce auditing and ethical standards, registered company auditors and similar professionals do indeed charge higher fees than other SMSF auditors.

The potential impact of non-audit services on auditor independence has been a cause of worldwide regulatory concern over the past decade. In Australia, the Cooper Review addressed this issue, with one of its 15 recommendations for the SMSF sector taking the form of an objection to the joint supply of non-audit and audit services.

However, a counter argument is that joint supply of audit and non-audit services enables the auditor to know the client better, suggesting benefits in the form of knowledge spill overs.

This study finds audit partners providing non-audit services gain a greater understanding of the client, which appears to encourage, rather than inhibit, the reporting of breaches in the SMSF setting.

Accordingly, the study evidence appears to negate two concerns raised by the Cooper Review in relation to auditor independence. The study finds:

- Compliance standards in the audit industry appear high, evidenced by low levels of breaches and audit qualifications; and
The joint supply of non-audit and audit services and services bundling to SMSFs poses no threat in terms of auditor independence.