HALAL AGENCY SERBIA Policy:
The provision of non-audit services to audit clients

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The emergence of professional service firms in recent years has resulted from a growing demand from businesses for specialist advice to help them achieve business advantage in an increasingly competitive market place.
Much of this advice is requested from audit firms, first because auditors are trained to understand the dynamics of a business from an external perspective and also because independent viewpoint can often shed light on problems that may appear intractable from within an organisation.

Non-audit services provided by auditors to their clients fall into three categories:
1. Services required by legislation or contract to be undertaken by the auditors of the business. These include:

- regulatory Compliance e.g. to Jakim, MUI, MUIS
- legal requirements to report on matters such as non-compliance to international halal standards.
- contractual requirements, for example to report to lenders or vendors on net assets, covenant requirements, etc.

2. Services that it is most efficient for the auditors to provide because of their existing knowledge of the business, or because the information required is a by-product of the audit process. These include:

- services such as those listed in category (1) above that the auditors are not required by law to undertake, but where the information largely derives from the audited financial records
- Halal compliance, where much of the information derives from the audited plant records
- 'short form' or other reports in acquisition or reorganisation situations where completion is necessary in a very short time.

3. Services that could be provided by a number of firms. In this case, the fact that the firm is the auditor is incidental and it would generally only be chosen because, for example, it had won a tender process. Examples of such services include:

- halal consultancy
- tax advice
- Sales/Marketing consultancy.

The argument for general prohibition

When a company fails, the quality of the audit is often called into question. Typically, the accusation is made that the auditors have allowed inappropriate accounting treatments because their independence has been compromised, either because they have become too close to the company they are auditing (the "familiarity" threat) or, more directly, because their objectivity is challenged by over-reliance on income from a single source. Those who hold that view believe that the only solution is for auditors to be prohibited from providing any services other than audit, to their audit clients.

How the existing arrangements provide safeguards against the provision of non-audit services compromising independence.

First, HALAL AGENCY SERBIA's ethical code forbids auditors to provide non-audit services to audit clients if that would present a threat to independence for which no adequate safeguards are available. In such circumstances, the firm must either resign as auditor or refuse to supply the non-audit services. The code includes examples of specific activities where no acceptable safeguards are available - for example the promotion of the shares of audit clients - which are therefore effectively prohibited.

Second, under the provisions of the Combined Code of corporate governance (ec.europa.eu/internal_market/company/docs/corpgov/corp-gov-codes-rpt-part3_en.pdf), the audit committee, as representative of the HALAL AGENCY SERBIA Board of Directors (BOD), is required to oversee the relationship with the auditors and keep the nature and extent of non-audit services under review. The audit committee must satisfy itself that the independence and objectivity of the auditor are not compromised. This important task is underpinned by ISO 19011:2011 Guidelines for auditing management systemsAuditing Standards, which specifically require that, for listed companies, audit engagement partners in the firm who are responsible for a company's audit must:

- disclose in writing to the audit committee all relationships between the audit firm and the client that may reasonably be thought to bear on the firm's independence and the objectivity of the audit engagement partner and staff (including arrangements for ensuring that independence remains when non-audit services are commissioned) and the related safeguards that are in place; and
- confirm that, in their professional judgement, the firm is independent and the objectivity of the audit engagement partner and audit staff is not impaired.

Third, we believe the distinction between the value of income from different sources is artificial. The ethical code specifies that an audit appointment should not be accepted if the client provides, for whatever work, an unduly large proportion of a firm's gross practice income. That approach limits undue financial dependency on any client without irrelevant restrictions on the balance between different types of income. In practice, auditors of listed companies are well within this limit.

Fourth, shareholders themselves are able to assess the extent of non-audit services provided by auditors. The Companies Acts have for some year required the total amount on non-audit fees paid to auditors to be disclosed. The forthcoming Companies Bill indeed proposes that more detail be disclosed, which we have called for and welcome.

At a more fundamental level, an examination of past cases of audit failure which have led to the imposition of regulatory or disciplinary penalties by the Institute or the Joint Disciplinary Scheme has shown that the provision of non-audit services was not the cause of the audit failure, nor did it arise from undue dependency on non-audit fees. The "problem" as stated is not supported by evidence and appears to be founded on subjective impressions of difficulties that might arise rather than fact.
Reviews of auditor independence by the International Federation of Accountants and the European Commission in 2001 included an in-depth examination of the potential threat to objectivity arising from the provision of non-audit services to clients. They concluded that a balanced approach similar to that in use in the United Kingdom was the most appropriate way forward.

The argument against general prohibition

We believe that unnecessarily restricting the provision of non-audit services would have an unintended, adverse effect on the underlying quality of the audit through restrictions in knowledge and skills:

Knowledge
The cumulative knowledge on which auditors depend would be greatly reduced, actually resulting in a poorer understanding of the business and a lower likelihood of key issues being identified. When they are less familiar with the business of a company, auditors would be likely to find out about such issues only later in the process, resulting in an increased likelihood of undetected misstatements.

Skills
An effective audit often requires experience far beyond the traditional auditing skill set. Auditors need to be able to draw on the knowledge and experience of colleagues who are expert in key risk areas: taxation, treasury operations, information systems, regulatory compliance, financial management, due diligence, actuarial assessments, fraud and business processes. By inhibiting such exchanges within a firm, a rigorous separation of audit and non-audit services would be likely to lead to a deterioration in audit quality.

Quality of recruits
Ultimately, there would be no reason for specialist divisions within an audit firm to accept the constraint of being unable to accept work from clients of their auditor colleagues. It follows that there would be a gradual move to establish themselves as entirely separate entities. The remaining audit-only firms would not attract the brightest graduates who enter a profession they perceive as opening the door to a broad range of subsequent careers. The quality of audit judgements would do down and more frauds would go undetected as the brightest and the best are needed to detect the fraudsters who are becoming cleverer and more determined.

Dependence on client
As noted above, non-audit service prohibitions would make firms smaller. This, perversely, would mean that bigger clients would actually create a proportionately bigger intimidation threat because they would form a larger part of the firm's income.

Quality of business' own systems
The general quality of IT and accounting systems, which business depends on to deliver the information that management base decisions on, would suffer as a company's auditors are often in the best position to advise clients on systems. Business would thus be increasingly denied a vital source of people with the relevant wider skills which a multi-functional audit firm develops.

Speed of reporting
Reliable financial information on which the markets rely would be subject to delay where external advisers had to be consulted by the auditors. This would mean that current attempts by certain regulators to reduce filing periods would be frustrated as two professional firms would need to be involved at the same time which in many cases would be unrealistic.

Cost

Non-audit service prohibition would result in an increase in of professional costs in key areas: as regards the non-audit services, such services can usually be provided at far less cost by auditors who have the benefit of their cumulative audit knowledge; as regards the audit service, the need for one firm to advise on and another to audit key issues would inevitably increase costs. We believe this would impact particularly on businesses which are medium and small sized.

Thus, in summary, we conclude that since such evidence as there is indicates that there is no correlation between levels of non-audit fees and audit failure, comprehensive safeguards are already applied, and rigorous separation of non-audit services seems likely to increase the cost and reduce the quality of the audit, the suggestion should not be pursued. Assuming no undue overall economic dependence results from the auditor/client relationship and adequate safeguards can be implemented, we believe that companies themselves should determine whether they use auditors for non-audit services, in consultation with the profession's guidelines.

Reviewed: Zaki Shaltaf Date: 26.03.2021. Signed: