



Kate Dalby
Financial Reporting Council
8th Floor
London Wall
LONDON
EC2Y 5AS

Grant Thornton UK LLP
30 Finsbury Square
London
EC2A 1AG
T +44 (0)20 7383 5100

15 January 2024

Dear Kate

Proposal to revise the ISA (UK) 250 (Revised), Consideration of Laws and Regulations in an Audit of Financial Statements and ISA (UK) 2X0 (Revised), Special Considerations for Public Interest Entities – Communicating and Reporting to an Appropriate Authority Outside the Entity

Grant Thornton UK LLP (Grant Thornton) welcomes the opportunity to comment on the Financial Reporting Council's (FRC) proposal to revise ISA (UK) 250, Consideration of Laws and Regulations in an Audit of Financial Statements (ED-ISA (UK) 250) and ISA (UK) 2X0, Special Considerations for Public Interest Entities – Communicating and Reporting to an Appropriate Authority Outside the Entity (ED-ISA (UK) 2X0).

We appreciate the steps that the FRC are taking to support the delivery of high quality audit and assurance work to maintain investor and wider stakeholder confidence in audit and assurance.

We have the following views on the two standards:

- We have a number of concerns with the proposed changes to ED-ISA (UK) 250 (extant ISA (UK) 250 Section A) and the impact these changes have on the scope of an audit. We have set out these concerns and alternative ways forward in Appendix A. We are concerned that the risk assessment and response as drafted fundamentally changes the scope of the audit within the UK and globally for listed multinational UK companies.
- Overall, we are supportive of the enhanced requirements in respect of changes proposed to ED-ISA (UK) 2X0 (extant ISA (UK) 250 Section B). However, we do believe the definition of reportable matters should be revisited and have provided a suggestion to align the definition with well understood terminology already used in the ISAs. We have also queried the benefit of reporting such matters in the absence of a corporate regulator (similar to the Securities and Exchange Commission (SEC) in the US).

We also strongly recommend that the FRC undertakes further outreach with a variety of stakeholders, including audit committees, financial statement preparers, and those in legal and regulatory professions to obtain their views on the changes proposed based on concerns raised.

Our detailed responses to the FRC's questions in the Exposure Draft are set out in Appendix B. We have also included detailed drafting comments in respect of ED-ISA (UK) 250 and ED-ISA (UK) 2X0 in Appendix C. We would be pleased to discuss those responses with you. If you have any questions, please contact me.

Yours sincerely



Chris Smith
Partner, Head of NAS Grant Thornton UK LLP
T +44 (0)20 7728 3446
E Chris.smith@uk.gt.com

Enc

APPENDIX A

Summary of concerns in respect of proposed changes to ED-ISA (UK) 250 and alternative ways forward

We have summarised our concerns/matters for the FRC to consider in response to their proposed changes to ED-ISA (UK) 250 below.

Public interest

We are not aware of any pressing demand or public interest need to address an actual or perceived gap in the auditors work over laws and regulations. Examples of public interest matters have been listed in our response to question 1 (see Appendix B) for which there was no public challenge as to why the auditor had not identified these issues beforehand.

Further, we are of the view that adding new requirements or enhancing requirements in the current auditing standards on non-compliance with laws and regulations may in fact result in an expectation gap as more will be expected of the profession by stakeholders in this area than is intended by the FRC. This may result in increased risk of civil and other litigation where material losses are incurred following identification of non-compliance with laws and regulations which were not intended to be covered by ED-ISA (UK) 250.

Purpose of an audit

The underlying basis of an audit is that an auditor will perform their audit over a set of financial statements prepared in accordance with a reporting framework used by the preparer. The objective of a financial statement audit is to obtain reasonable assurance about whether the financial statements are materially misstated, whether due to fraud or error. An auditor is required to have the requisite knowledge of accounting and auditing. The auditor is not required to be an expert in laws and regulations and neither does an audit seek to provide assurance over the entity's compliance with laws and regulations. The level of work required to provide this additional assurance would be significant and hampered by the absence of a recognised framework for the preparer and lack of applicable assurance standards for the auditor (and associated experts).

We believe this is the basis under which the current ISA (UK) 250 Section A¹ distinguishes between direct and other laws and regulations. Further to this, the auditor will be required to:

- determine from the risk assessment and other activities whether there is an indication of a risk of material misstatement to non-compliance with laws and regulations and non-compliance or suspected non-compliance with laws and regulations;
- design and perform further audit procedures which are responsive to the determination above; and
- evaluate whether sufficient appropriate audit evidence obtained indicates there is a material misstatement relating to non-compliance with laws and regulations.

We, therefore, have concerns about whether the changes proposed to remove the distinction of direct and other laws and regulations inadvertently changes the assurance being provided in respect of an entity's compliance with laws and regulations. We believe the scope of an audit would inadvertently be expanded such that it also provides assurance on an entity's compliance with all laws and regulations to the point of not materially misstating the financial statements. This is akin to a supplementary assurance service over and above the financial statements audit.

Furthermore, with the removal of the distinction between direct and other laws and regulations, we cannot see the point at which auditors can reasonably and consistently draw a line in terms of work effort required in order to support the risk assessment which is proposed. This concern is also relevant to the potential for increased risk of civil litigation.

¹ ISA (UK) 250 (Revised November 2019) Section A - 'Consideration of Laws and Regulation in an Audit of Financial Statements

Expertise

The proposed changes to ED-ISA (UK) 250 require auditors to identify risks of material misstatement due to fraud or error relating to non-compliance with all and any applicable laws and regulations. In order to identify the laws and regulations with which non-compliance could reasonably have a material effect on financial statements, preparers and auditors would need to identify all the laws and regulations applicable to the entity. We believe it will be difficult for auditors to identify and assess all the laws and regulations under which non-compliance could reasonably have a material effect on an entity's financial statements without having to engage with lawyers and other experts to identify all relevant laws and regulations. Examples of other experts are those that would be required in mining, pharmaceuticals, engineering, housing and food production sectors. This is compounded by auditors being required to assess qualitative, not just quantitative, materiality in respect of actual and suspected breaches of laws and regulations. This assessment will be more difficult and may result in auditors erring on the side of caution when assessing how stakeholders would view suspected or actual breaches of laws and regulations. A case can easily be made that a breach is qualitatively material to at least some users of the financial statements, given it involves non-compliance with a law or regulation. This may have the unintended consequence of giving greater weight to breaches by virtue of their disclosure.

For the avoidance of doubt, we believe auditors will need to engage lawyers as well other related experts to perform audits in accordance with the proposed draft. Our understanding and experience is that compliance and regulatory experts would want to carry out a review before providing a view or report or opinion which would give rise to additional costs to the audited entity. This will result in significant costs and work effort on both preparers and auditors.

Management's assessment and responsibilities

While we note that the FRC, in discussion, has stated that the standard envisages that the risk assessment is based on that of management's assessment, we consider that the current drafting and principles of the auditing standards, as a whole, would require the auditor to make an independent assessment of management's assessment thereby placing a burden on the auditor to do so and to apply the appropriate skills and expertise.

In addition, we are unclear whether the FRC has considered the cumulative impact of multiple individually immaterial risks of non-compliance with laws and regulations. The auditor would have to consider whether the cumulative impact of breaches of laws and regulations is material or not, even though an individual breach of laws and regulations may not be material. This will also result in significant work effort in identifying all breaches of laws and regulations and the impact of this to the entity.

This verbal guidance (from the FRC) also does not address the varying quality of assessments which management of different entities will make in respect of relevant laws and regulations. It is common for growth phase immature companies to have less formalised internal controls than established listed companies and for auditors to address this through different audit approaches. The proposed standard and discussion has been silent on how auditors should address varying quality of such assessments performed by management. However, using the principles of the auditing standards, as a whole, it would surely fall on the auditor to require management to enhance their assessment and/or respond by performing additional work of their own.

This proposal does also increase the risk of modified audit opinions where auditors are unable to satisfy themselves with management's assessment of laws and regulations. Further, where management decide to impose a limitation of scope, auditors would then need to reconsider their appointment as auditor for such entities.

Work effort and cost

We are also of a view that the changes proposed in ED-ISA (UK) 250 will result in significant work effort and costs by, both, management and auditors. We are concerned that the unintended consequences of the proposal, including increased time and costs, would outweigh the perceived benefits.

We have considered the costs in a sample of recent audits where we have had to deal with matters pertaining to laws and regulations under the current auditing standard. In these scenarios, we found that the majority of audit fees increased by 15%-150% which far exceeds the estimates in the proposal document. Furthermore, the increased audit fees were exceeded by the costs incurred by audited entities on the various advisors used in respect of these matters.

We also believe that certain types of companies and sectors may become very difficult and particularly costly to audit at the appropriate quality level and certain auditors would consequently avoid such companies and/or sectors.

We would request the FRC to consider whether this impact is appropriate within the context of supporting the UK's economic growth and international competitiveness. We note the public letter from Kemi Badenoch's to the FRC's new CEO² in which she updates their remit which included the following statements:

"...the FRC should contribute to promoting the competitiveness and growth of the UK economy, embedding its growth duty across its work ..."

"Proportionality of any new requirements is essential and it is also important to look actively at where rules and guidance are no longer proportionate and can be removed or streamlined."

International

The FRC's response letter to the International Auditing and Assurance Standards Board's (IAASB) Consultation on ISA 250³ in 2016 suggested a more fulsome review of the standard in particular the distinction between the categories of laws and regulations. The IAASB decides its priorities based on the responses it receives to the strategy and work plan consultation and ISA 250 did not receive the support to be included in the workplan.

The Public Company Accounting Oversight Board's (PCAOB's) is also consulting on their equivalent auditing standard related to a Company's Non-compliance with Laws and Regulations and Other Related Amendments. They are also recommending similar changes, including removal of the distinction between direct and other laws and regulations and new and enhanced requirements to identify and assess the risk of material misstatement due to non-compliance of laws and regulation. We are aware that a large number of stakeholders have raised concerns with the PCAOB about the changes they have proposed and currently the outcome of the consultation has been delayed.

As such and further to the concerns raised in respect of the public interest, we would ask the FRC to consider the international environment in their decision making. It may be more sensible to allow another jurisdiction to lead in making significant changes in this area and review the impact of those changes, before opting to making changes to the equivalent standard in the UK.

Extra Territoriality

The proposed change will impact group audits by increasing the work required of component auditors of the group outside of the UK. Under the proposed changes group auditors will be required to have an understanding of and assess all laws and regulations that would impact components in the jurisdiction the components operate in. This in turn would also require component auditors to have an understanding of and assess all laws and regulations that apply in the jurisdiction (higher work effort required by ISA (UK) compared to ISAs issued by the IAASB) and to do this will require significant work effort and cost incurred by local management and component auditors outside of the UK. This could have a detrimental impact on the UK's attractiveness and competitiveness. It may also impact on auditor competition and choice as smaller firms may be less likely and/or able to audit international groups.

² [Letter from Secretary of State Kemi Badenoch to Richard Moriarty, CEO Financial Reporting Council, 22 November 2023 \(publishing.service.gov.uk\)](#)

³ ISA 250 'Consideration of Laws and Regulation in an Audit of Financial Statements'

Scalability

We are of the view that there are also scalability issues in relation to the application of ED-ISA 250 to entities of difference sizes, complexities and circumstances. The PCAOB's related proposal only applies to listed entities. However, the changes proposed in ED-ISA (UK) 250 apply to all entities where an audit is performed under ISAs (UK).

As mentioned above, the removal of the distinction of direct and other laws increases the work effort for both management and audit firms. Removal of this distinction also has an impact on the scalability of ISA (UK) 250 for medium and small sized entities. These entities are unlikely to have resource to identify, maintain and assess all the relevant laws and regulations (where this is deficient, auditors will need to perform additional work). The increased work effort from auditors is also likely to increase the audit fees charged to medium and small entities, as well as increased internal costs for companies to satisfy the audit requirements. As a consequence, owner managed businesses, with no external investors, are likely to suffer the most disproportionate impact from this proposal.

Alternative ways forward

Despite the concerns raised above, we do agree that auditors should consistently perform audit procedures to identify risks of material misstatement due to fraud or error relating to non-compliance with laws and regulations and perform audit procedures to address those risks.

To achieve this, we have included alternative suggestions below:

1. Include an additional planning requirement for auditors to consider breaches of laws and regulations that have resulted in material loss(es) in the sector in which the entity operates and whether that gives rise to a risk of material misstatement relating to non-compliance of laws and regulations for the entity.
2. Further enhance the risk assessment procedures to reflect the requirements of ISA (UK) 315 (Revised July 2020) (ISA (UK) 315)⁴ whilst retaining the distinction of 'direct and other laws and regulations'. This could for example include suggestion 1 above.
3. Include a requirement for auditors to assess the risk of material misstatement for instances of actual or suspected non-compliance with laws and regulations for both direct and other laws and regulations identified by the planning process.
4. Look to implement the recommendation from Sir Donald Brydon's Report of the Independent Review into the Quality and Effectiveness of Audit (Brydon Report)⁵ which would require directors to set out in a Public Interest Statement (as part of the strategic report) how they view the company's legal, financial, social and environmental responsibilities to the public interest. Once this is implemented, the FRC could then add audit responsibilities associated with the Public Interest Statement.

⁴ ISA (UK) 315 (Revised July 2020) 'Identifying and Assessing the Risks of Material Misstatement'

⁵ Assess, Assure and Inform, Improving Audit Quality and Effectiveness: Report of the Independent Review into the Quality and Effectiveness of Audit, paragraph 6.8.5

Responses to the Proposed ISA (UK) 250 (Revised), Consideration of Laws and Regulations in an Audit of Financial Statements and ISA (UK) 2X0 (Revised), Special Considerations for Public Interest Entities – Communicating and Reporting to an Appropriate Authority Outside the Entity

ISA (UK) 250—Consideration of Laws and Regulations in an Audit of Financial Statements

Q1. Do you agree that the proposals in ISA (UK) 250 appropriately address the public interest?

We are unclear what issues and public interest needs the FRC are seeking to address with this consultation. While we accept this standard is more procedural and less principles based than others, we do not see this in of itself to be a driver for change given the auditor is not expected to be an expert in laws and regulations.

Furthermore, it is unclear what findings from audit quality and thematic reviews (such as the Audit Quality Thematic Review – Fraud risks and laws and regulations) the changes are trying to address.

- From reviewing recent reports detailing the findings from the Audit Quality review team there are no findings in respect of non-compliance of laws and regulations that suggest the standard should be revised. Findings from the Audit Quality reviews⁶ show that that auditors identified non-compliance of laws and regulations as a risk of material misstatement however may have not performed sufficient audit work to address the risk identified.
- The matters raised in the Audit Quality Thematic Review – Fraud risks and laws and regulations mostly relate to audit teams' application of these requirements in practice and did not identify any significant deficiencies which indicated that an inappropriate audit opinion may have been issued.

Both of these findings indicate that more direction could be provided in responding to instances of actual or potential breaches of laws and regulations, however this is not addressed in the consultation.

The Brydon Report included a recommendation for directors to set out in a Public Interest Statement (as part of the strategic report) how they view the company's legal, financial, social and environmental responsibilities to the public interest. This statement should explain how the company has discharged its self-declared interest obligations and responsibilities, what actions it has taken to mitigate any externalities it has caused during the period, and how effective these actions have been. The report also explains that the information included in the statement should not be an exhaustive summary of every legal duty but that the company or its directors comply with, but rather a concise explanation by the directors of how they perceive the public interest in their company and how they have taken measures to serve that interest over the previous year.

The information included in the report would suggest that if the company considers legal duties that the directors perceive are in the public interest, then the auditor also considers those laws and regulations impacting an entity that may be perceived to be of public interest. In the absence of such changes made to directors' responsibilities, we do not see the benefit of making changes now. Furthermore, were directors' responsibilities enhanced, the auditing standard could be changed to address those changes specifically.

We have also considered the public interest need further, in particular given audit and governance reform proposed and actioned in the UK. This reform was driven by corporate failures and

⁶ Key Findings Reported in 2020/21 Inspection Cycle and BDO LLP Audit Quality Inspection and Supervision

stakeholder concerns that the underlying audits were not of the appropriate standard. This environment has not changed in the UK with continued scrutiny of auditors where there are significant concerns or failures of UK corporates. This is evidenced most recently by the questions asked by the parliamentary select committee following the collapse of the UK retail chain Wilko Limited. Wilko Limited was audited by Ernst and Young LLP, who for the avoidance of doubt had issued an audit opinion with a material uncertainty related to going concern prior to the company going into administration.

However, despite this scrutiny over the role of the auditor, we note the following matters involving laws and regulations which materially impacted the entities for which subsequently there was no concern raised in respect of the financial statements audit by stakeholders:

Entity impacted	Matter involving breach of laws and regulations	Link to further information
Thames Water, Wessex Water and Southern Water	Pumping raw sewage into the environment is permitted only when firms are dealing with "unusually heavy rainfall". But the investigation found that three water companies collectively released sewage in dry spills for approximately 3,500 hours throughout 2022, in violation of their permits.	UK's biggest water companies accused of illegal dumping of sewage during dry days The Independent
Royal Borough of Kensington and Chelsea ('Grenfell')	Since the Grenfell fire, repairs have been required to buildings with unsafe cladding. This has impacted various entities that have used unsafe cladding.	Unsafe cladding: What is it and who pays to remove it? - BBC News
Volkswagen	The Environmental Protection Agency (EPA) found that many VW cars being sold in America had a "defeat device" - or software - in diesel engines that could detect when they were being tested, changing the performance accordingly to improve results. The German car giant has since admitted cheating emissions tests in the US. While there was an element of fraud in this example, it involved non-compliance with regulations.	Volkswagen: The scandal explained - BBC News
Ikea ('horse meat scandal')	The Food Safety Authority of Ireland tested a range of cheap frozen beefburgers and ready meals from supermarkets last November for the presence of DNA from other species which were undeclared. It found horse DNA in over one-third of	Horsemeat scandal: the essential guide Horsemeat scandal The Guardian

	the beefburger samples, and pig in 85% of them.	
Bernard Matthews ('turkey scandal')	It was identified that turkey escalopes or sandwich meat had come from Brazil, or Hungary, or Poland; anywhere in the world. But as long as it is processed in Britain, it can bear a British hallmark under which turkey products were sold by Bernard Matthews.	Grubby scandal shames our poultry industry Health The Guardian
BHP ('dam collapse')	BHP Group potentially faced a 36 billion pound (\$44 billion) lawsuit in London over Brazil's worst environmental disaster after the number of claimants more than tripled to 700,000 following the collapse of the Fundao dam, owned by the Samarco joint venture between BHP and Brazilian iron ore mining company.	Miner BHP potentially faces \$44 bln bill in Brazil dam case Reuters
BP ('deepwater horizon')	The oil drilling rig <i>Deepwater Horizon</i> , operating in the Macondo Prospect in the Gulf of Mexico, exploded and sank resulting in the death of 11 workers on the Deepwater Horizon and the largest spill of oil in the history of marine oil drilling operations.	Deepwater Horizon – BP Gulf of Mexico Oil Spill US EPA

All of these examples raise the following questions and concerns:

- does the FRC believe the proposal will result in preparers and auditors identifying such matters in advance of them taking place. If the FRC do not believe this is the case, the FRC will need to ensure the proposal more clearly addresses this scope question and that stakeholders understand where the responsibility of an auditor ends in the context of an entity's compliance with laws and regulations.
- subsequent lack of challenge by stakeholders of the audit in these examples points to an understanding that an audit cannot capture every business risk (including compliance with laws and regulations) and nor should it. The FRC needs to carefully consider expanding the auditor's role in relation to laws and regulations through this proposal as it risks creating an expectation gap as to what an audit can reasonably achieve.

Q2. Do the proposed requirements in paragraphs 12-2–12-3 support auditors to be able to identify those laws and regulations with which non-compliance may have a material effect on the financial statements?

We are of the view that the requirements included in paragraphs 12-2 – 12-3 will support auditors in identifying those laws and regulations with which non-compliance may have a material effect on the financial statements by enhancing the requirements and providing some specificity in this regard.

Notwithstanding our agreement, we:

- refer you to our concerns set out in Appendix A of this letter.
- are of the view that the requirements in extant ISA (UK) 315 already requires auditors to enhance their planning effort in relation to laws and regulations given the interrelated nature of the auditing standards (see ISA (UK) 315.19.(a)(ii)).

In our experience this is evidenced by the work auditors undertook post Grenfell in the Housing Association sector which required them to understand and challenge how management of Housing Associations had understood and assessed compliance with relevant laws and regulations in regard to cladding and their housing portfolio. Interestingly, ISA (UK) 315.A70 only suggests auditors consider '*Legislation and regulation that **significantly** [emphasis added] affect the entity's operations*' which serves to illustrate the difference in scale of enhanced effort proposed by the FRC in this consultation versus that already required.

Other comments:

- We also note that paragraph 12-1 has moved beyond that which is required under paragraph 12 of the extant standard. In paragraph 12 of the extant standard, the auditor is required to obtain a 'general understanding' of the legal and regulatory framework and compliance thereof. In our view, this recognises that the auditor does not need to be a legal or regulatory expert outside of the direct laws which impact a business. However, paragraph 12-1 proposes to do away with that and enhances the extant requirement significantly in respect of laws and regulations. This change goes beyond the expertise of an auditor and increases the scope of an audit significantly. This is most prevalent for indirect laws and regulations.
- Paragraph 12-3 (b) (iv) requires inspecting 'such other records or documents as the auditor considers necessary...'. We are of the view that this paragraph creates a requirement for auditors to inspect any record or document that could indicate any indication of non-compliance with laws and regulations. If this requirement is retained, we recommend that application material is included addressing what records and documents should be inspected and the extent of records and documents an auditor is expected to inspect to meet this requirement.
- Currently there is no standardised requirement for management to prepare and maintain a list of all laws and regulations relevant to the entity and assess the risk of a potential material misstatement in this regard. Without a requirement for management to address the risks arising from laws and regulations, it may become difficult for auditors to perform these procedures and may result in the audit being a driver of an additional process on business. We also note that a fundamental element of assurance is that the preparer will use a framework, which the assurance provider will then perform work over. In this regard there is no such standardised framework. Furthermore, this comparison also demonstrates the risk that some stakeholders may think auditors are providing an opinion on 'material compliance' with laws and regulations.
- If the FRC go ahead with the proposed changes, we are of the view that entities will spend significant amounts of time and money to facilitate the required audit effort. Entities with or without inhouse legal teams will have to engage solicitors and other experts to help them identify and assess all laws and regulations. For the majority of sectors and industries, auditors are unlikely to have the necessary knowledge to identify and assess all laws and regulations and therefore will also be required to engage experts.

Q3. Do you believe that the proposals in ISA (UK) 250, considered collectively, will enhance and strengthen the auditor's identification of risks of material misstatement of the financial statements due to fraud or error relating to non-compliance with laws and regulations?

The changes proposed extend the scope of an audit and are likely to result in both auditors and entities spending significant amounts of time and incurring significant costs to identify and assess all relevant laws and regulations, which may also lead to an expectation gap as set out in the covering letter/Appendix A and questions 1 and 2 above. We, therefore, cannot support the current proposal

We also have concerns in regard to the application of paragraph 14-1. The proposed requirement will require the auditor to determine whether the audit evidence obtained from risk assessment procedures indicates a risk of material misstatement relating to non-compliance of laws or regulations or non-compliance of or suspected non-compliance with laws and regulations. The extant standard requires auditors to obtain sufficient appropriate audit evidence regarding compliance with provisions of those laws and regulation generally recognised to have a direct effect on the determination of material amounts disclosed in the financial statements. The proposed change increases the scope of the requirement and would require auditors to have or engage with experts of laws and regulations to determine risks of material misstatement relating to non-compliance with laws and regulations.

To address this concern raised, we recommend the following change to paragraph 14-1:

“In applying ISA (UK) 315, the auditor shall determine whether the risk assessment procedures (including the preceding requirements) and any related activities indicates the existence of a risk of material misstatement due to fraud or error relating to any instances of non-compliance or suspected non-compliance that the auditor has become aware of”

We believe that anchoring the risk assessment to instances of actual or suspected instances of non-compliance with laws and regulations will mitigate the burden imposed by the current proposals, but still clarify audit responsibilities in this area.

Q4. Have appropriate enhancements been made to the application material?

Further examples and guidance should be provided to ensure consistent application of the proposed requirements. The examples and guidance are required to illustrate the extent of work required to identify laws and regulations and assess whether it will have a material impact on the financial statements.

In particular, given the scope of the proposed changes the FRC could also use the application material to describe what is and what is not expected under the new requirements.

Q5. Do you support the deletion of the Appendix on “Money laundering, terrorist financing and proceeds of crime legislation in the United Kingdom”?

The Appendix on ‘Money laundering, terrorist financing and proceeds of crime legislation in the United Kingdom’ provides useful information to the auditor on their responsibilities that arise as a result of money laundering, terrorist financing and proceeds of crime.

We are of the view that the Appendix can be deleted and the information contained in the Appendix is published elsewhere that is easily accessible and a clear reference of its published location is included in the revised ISA (UK) 250.

Q6. Do you agree with the proposed effective date for audits of financial statements for periods commencing on or after 15 December 2024?

We do not believe that ED-ISA (UK) 250 should be issued with the changes proposed and strongly recommend and request that the FRC address the concerns raised by audit firms and other stakeholders. In particular, the FRC should carry out further outreach with investors, companies (across different sizes and types of entities) and other relevant stakeholders as the proposed changes are likely to have an impact of the work effort required (both entities and auditors) and costs incurred.

As mentioned above, we also recommend waiting for the results of the PCAOB consultation outcome, given the scale of changes being proposed. It might be better to allow other jurisdictions to implement similar changes and learn from their post-implementation reviews, rather than be the first to implement the changes proposed.

ISA (UK) 250 —Special Considerations for Audits of Public Interest Entities—Communicating and Reporting to an Appropriate Authority Outside the Entity

Q7. Do you agree that the proposals in ISA (UK) 250 appropriately address the public interest?

The changes to this ISA (ED-ISA (UK) 2X0 (extant ISA (UK) 250 Section B) are driven by the Sir John Kingman report⁷ and we are of a view that the changes proposed conceptually address the public interest. However, we have noted a few concerns in our responses to the detailed questions below.

Q8. Do you agree with the proposed scope of ISA (UK) 250 being limited to public interest entities, or do you believe that the requirements of ISA 250 should also apply to: a) Listed entities b) Charities c) Other entities in regulated industries d) All entities. When responding consider that for many audits, as reportable matters are not likely to be identified, only the requirements in paragraphs 11 – 13 will apply and that all auditors are subject to anti-money laundering legislation.

We are of the view that ISA (UK) 2X0 should not be applicable to all entities and should be applicable to PIEs and regulated entities only.

Regulated entities (that may not meet the definition of a PIE) already have requirements from their regulators to report matters and these requirements are likely to take precedence over any reporting requirements if the ISA was applicable to any such entities. Furthermore, there is an existing regulator for auditors in these sectors to report to and they have powers over entities in their sector.

If the requirements were to be extended to other entities or all entities, it is not clear who auditors would report matters to and what action would be taken, if any, in respect of UK companies. We are of a view that without a corporate regulator with associated powers there may be little benefit in an auditor reporting matters to another regulator. To address this concern, we would suggest that a corporate regulator is required for this proposal to have a substantial and positive impact. The corporate regulator would operate within a regulatory framework that would allow auditors to report matters freely within such a framework.

In our view, it is also likely that many breaches qualifying as Reportable Matters will have been investigated by an audited entity under the cloak of legal professional privilege, which is unlikely to be waived by the entities for our purposes of reporting to a relevant regulator. Under current law, reporting requirements in the ED-ISA would not override the audited entity's right to privilege, which could lead to either incomplete reporting, or reporting which could not properly inform the appropriate authority of the matter being reported.

Q9. Do you support the definition of Reportable Matters?

It is essential to have clarity on the threshold for reporting matters in the public interest, given the possible consequences on auditors in respect of financial losses arising from matters which could later be said to have been avoidable had the auditor reported suspected or actual non-compliance, as set out in A59 of the proposed Application Guidance.

We are of the view that the definition of reportable matters is not clear, specifically in respect of the 'such significance that is in the public interest to report...'. Interpreting the term 'significance' is judgemental and likely to be interpreted differently by auditors which would lead to inconsistent application of the requirement to report matters.

In addition, we think that it is difficult to determine what matters would not be in the 'public interest'. In so far as a breach of laws or regulations go, it is not difficult to make the case that they are in the public interest. For example, out of 100 people, say, it is likely that at least one person would find a matter of 'public interest'. We recommend that further guidance is included in the application material to help determine what matters would be in the public interest, and importantly, what matters wouldn't be in the public interest, to ensure this definition of Reportable Matters is consistently applied.

We would recommend the term 'pervasive' rather than 'significance' and 'public interest' is used as this is a concept that already exists in the ISAs. We do not think 'material' should be used in the

⁷ Independent Review of the Financial Reporting Council by Sir John Kingman - Recommendation 45 – The review recommends that the Government introduces a duty of alert for auditors to report viability or other serious concerns.

definition of reportable matters⁸ as this could potentially bring in a number of matters into the scope of the definition of reportable matters which may be quantitatively material but may not be in the public interest to report.

We also recommend that examples of how this term is applied are included in the application material or the appendix to the ISA.

We would also request that the FRC consider what action is likely to be taken for reportable matters by the relevant regulator in determining whether the definition is appropriate.

Q10. Do you believe that the proposals in ISA (UK) 250, considered collectively, will enhance and strengthen the auditor's identification of matters that should be reported to an appropriate authority outside the entity?

We are of the view that the changes proposed to ISA (UK) 2X0 will enhance and strengthen the auditor's identification of matters that should be reported to an appropriate authority outside the entity. However, it is unclear who these matters would be reported to. Currently the FRC and other regulators with some/specific remits over corporates have limited powers over companies and their directors to address matters that may be reported to them by auditors. As suggested in question 8, having a corporate regulator would provide a better framework for matters to be reported and dealt with appropriately.

In the US, matters identified by the auditor in respect of audits conducted under PCAOB standards are reported to the SEC. The SEC is an oversight agency responsible for regulating the securities markets and protecting investors. We have observed the benefits of the US corporate reporting ecosystem regulatory model, where the corporate regulator, the SEC, is able to hold companies and directors to account, as well as overseeing the PCAOB, which regulates the auditors. This leads to more co-ordinated regulatory changes across the entire corporate reporting ecosystem and is the type of environment which would better suit the proposed changes.

Q11. Have appropriate enhancements been made to the application material?

We are of the view that the application material includes appropriate enhancements subject to our recommendation that further guidance and examples of reportable matters are included in application material, or staff guidance is provided to assist auditors in determining reportable matters.

Q12. Do you agree with the proposed effective date for audits of financial statements for periods commencing on or after 15 December 2024?

We are of the view that the effective date of ISA (UK) 2X0 could be brought forward however it makes sense to align the effective date with the ISA (UK) 250 Section A. As recommended in question 8, we are of the view that it would be even better to align the effective date of the ISA with the establishment of a corporate regulator in the UK.

We are consequently of the view that the implementation of ED-ISA (UK) 2X0 would be more effective if the UK had a SEC equivalent regulator.

⁸ 'Material' is used in ED-ISA2X0 paragraph 17(a)(i) and (ii).

Appendix C

Detailed drafting comments in respect of the Exposure Draft of ISA (UK) 250

Detailed below are our more detailed drafting comments:

ISA (UK) 250

Paragraph A6-1 makes reference to ISA (UK) 290 incorrect reference

Paragraph A29-1 makes reference to 'The Appendix contains further guidance' however the FRC propose on deleting the Appendix

Paragraph A29-3 makes reference to Section B should be changed to ISA (UK) 2X0