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By email to: AAT@frc.org.uk

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Dear Kate

Invitation to comment – Proposed International Standard on Auditing (UK) 250 (Revised) *Consideration of Laws and Regulations In An Audit of Financial Statements* and Proposed International Standard on Auditing (UK) 2X0 (Revised) *Special Considerations For Public Interest Entities—Communicating And Reporting To An Appropriate Authority Outside The Entity*

1. This is a response from UKSA (United Kingdom Shareholders' Association) to your invitation to comment on the proposed International Standards on Auditing (UK) (ISAs (UK)) 250 and 2X0 (Revised). As you would expect from the nature of our membership outlined below, the subject of external audits and therefore audit standards is of great importance to our members. We are reasonably clear on what we want and expect of audits and our comments are based on our professional experience as users of corporate reporting. However, please recognise that we are generalist audit report recipients and not technical experts in audits.

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A. Summary of our key points

2. Our key points are:

- 2.1. An entity or preparer, its management and those charged with its governance are primarily responsible for identifying those laws and regulations with which non-compliance may have a material effect on the financial statements
- 2.2. It is not an auditor’s responsibility to identify those laws and regulations with which non-compliance may have a material effect on the financial statements. Their responsibility is to assess an entity’s ability to have identified these laws and regulations and report to shareholders accordingly, and
- 2.3. The first objective at proposed paragraph 11-1 a) needs to change to reflect these points. We agree with your recognition that the auditor’s responsibilities cannot be open-ended and believe this is best effected by giving clear lines of responsibility between an entity and its auditors.

3. We would also like to highlight our disappointment with the government recently shelving audit and governance reform proposals on audit and assurance policies. Actively engaged individual investors provide an additional challenge to an entity, its management and those charged with its governance and are used as such by enlightened directors and management. This is also proving to be the case with auditors. Audit standards should prompt auditor engagement with investors.

B. About UKSA (United Kingdom Shareholders' Association)

- 4. UKSA represents the views of individual investors. We have around 12,000 members. In addition to our own members, 12 to 13 million people own shares or have investment accounts with platforms in the UK.
- 5. The Office for National Statistics estimates that at the end of 2018 UK-resident individuals held 13.5% of the UK stock market, up by 1.2% from 2016 and moving away from the historical lows of 10.2% in 2008. In 2020, the Financial Times estimated that 15% of the UK stock market is held by individual shareholders resident in the UK. In addition to this there are many more who

have money invested in shares via funds, pensions and savings products such as employee share ownership schemes.

6. UKSA was originally formed to provide individual shareholders with a voice, influence and an opportunity to meet like-minded fellow investors. It is structured as a non-profit making company with annual subscriptions. An elected Chairman and Board of Directors (all volunteers and individuals with a wide range of backgrounds and experience) monitor a regional organisation. Each region benefits from oversight by an elected regional Chairman and Committee.
7. There are many agents and intermediaries in financial markets. Unlike them, UKSA represents solely those people who are investing their own money. See www.uksa.org.uk

C. Consideration of laws and regulations in an audit of financial statements

8. At one of your recent roundtables on the proposed revisions to ISA (UK) 250 Section A and ISA (UK) 250 Section B, at which there were mainly preparers and auditors (not a lot of investors), two main things struck one of our members:
 - 8.1. An audit committee NED saying he felt like a turkey voting for Christmas when he suggested that responsibility for not complying with legal and regulatory requirements (NOCLAR) in financial reporting rests with company boards, and
 - 8.2. Some auditors worrying about what exactly was required of them under the standards.
9. As a result, it made us consider what exactly would we be looking for in respect of NOCLAR from our auditors when they audit and report to us on our investments. Our expectations would include:
 - 9.1. internal controls and processes (around ensuring compliance with applicable laws and regulations (CLAR)) are robust enough to prevent any material misstatements in financial statements
 - 9.2. material impacts from NOCLAR by entities outside of a preparer, such as material breaches of a preparer's intellectual property protections by these other entities, should be included in these CLAR internal controls and processes
 - 9.3. an auditor assessment of these CLAR internal controls and processes
 - 9.4. if such internal controls and processes are found to be reliable from an audit perspective, the audit report confirming this, and
 - 9.5. if the auditor finds the internal controls and processes to be unreliable and there are inadequate or no mitigating relevant disclosures in an

annual report, the audit report explaining the material deficiencies and the resulting risks of misstatement in financial statements.

10. The resulting key points from our expectations are:
 - 10.1. An entity, its management and those charged with its governance are primarily responsible for any consideration of laws and regulations in the preparation of financial statements and other corporate reporting
 - 10.2. An auditor, like the entity's investors (shareholders), should be able to rely on this primary responsibility and, if they prove to themselves through their audit that they can so rely, they can report such to their shareholders, and
 - 10.3. If they cannot, they should ensure that in the financial statements or elsewhere in an annual report, including their audit report if necessary, there are sufficient explanations and disclosures of relevant information to enable shareholders to assess the risk of any material misstatement in the financial statements from NOCLAR.
11. With these comments in mind, we support your explanations in your 'invitation to comment' document for your proposed changes, in particular removing any distinction between different categories of laws and regulations and making the auditing standard more closely aligned with an outcomes based approach. However, we are not sure the proposed revised ISA (UK) goes far enough in making an entity, its management and those charged with its governance primarily responsible for identifying those laws and regulations with which non-compliance may have a material effect on the financial statements. These are the people who would be expected to or should know as they are closest to the business model; not auditors nor investors (unless part of those charged with an entity's governance). Therefore the first objective in paragraph 11-1 a) needs to change, as it should not be an auditor identifying the relevant laws and regulations. **We suggest 11-1 a) is changed to 'to obtain from those responsible in an entity a list of the laws and regulations with which non-compliance may have a material effect on the financial statements'**. Also, the auditor, applying continuing professional scepticism, will need to assess the reasonable completeness of this list.
12. This consultation has reminded us that we were hoping that corporate audit and governance reform, started by the Kingman Review over five years ago, would lead to more auditor engagement with investors. Actively engaged individual investors provide an additional challenge to an entity, its management and those charged with its governance and are used as such by enlightened directors and management. This is also proving to be the case with auditors. Therefore we were disappointed by the government shelving recently the proposals for audit and assurance policies, which may have been a catalyst for increasing dialogue between boards, auditors and shareholders. **Audit standards should prompt auditor engagement with investors.** As we have mentioned elsewhere, this may not apply to consideration of laws and regulations due to the usual remoteness of investors from any business they have invested in.

D. Special Considerations for Public Interest Entities—Communicating and Reporting to an Appropriate Authority Outside the Entity

13. As our interest is the use of corporate reporting, we have not spent a lot of time on proposed ISA (UK) 2X0 (Revised). Therefore, we have no specific comments on the proposed auditing standard and have answered your questions on it briefly where we felt able to.

E. Answers to your specific questions

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

Question 1

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

14. Yes.

Question 2

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?

15. Yes. However, the objectives of the auditor set out in paragraph 11-1 need to reflect that it is not the auditor's responsibility to identify those laws and regulations with which non-compliance may have a material effect on the financial statements. This responsibility rests with the entity, its management and those charged with its governance. **We suggest paragraph 11-1 (a) is changed to 'to identify those laws and regulations identified by an entity, its management and those charged with its governance, with which non-compliance may have a material effect on the financial statements'.**

Question 3

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?

16. Yes.

Question 4

Q4 Have appropriate enhancements been made to the application material?

17. We cannot answer this question as not being auditors we have not assessed the enhancements to the application material.

Question 5

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

18. We are not sure audit report users like us should answer this question. Your ‘Invitation to Comment’ does not appear to explain your reasoning behind deleting this appendix to this ISA (UK). We assume that the deletion is because of the main reason for revising the audit standard i.e. making it more outcome focused and less overly procedural. If this assumption is right, we support the deletion on the basis that any auditor requirements are better dealt with elsewhere.

Question 6

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

19. Yes, as early adoption will be permitted. However, should not the revised ISA (UK) say that early adoption is permitted in the ‘Effective Date’ paragraph 10?

ISA (UK) 2X0—Special Considerations for Audits of Public Interest Entities—Communicating and Reporting to an Appropriate Authority Outside the Entity

Question 7

Q7 Do you agree that the proposals in ISA (UK) 2X0 appropriately address the public interest?

20. Yes, but see our answer to Q8 below.

Question 8

Do you agree with the proposed scope of ISA (UK) 2X0 being limited to public interest entities, or do you believe that the requirements of ISA 2X0 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.

21. No, ISA (UK) 2X0 should not just apply to public interest entities (PIEs). It should apply to d) all entities as this will make it simpler for all qualified auditors to consider the auditing standard when carrying out an audit, whether or not paragraphs 11-13 apply or not.

Question 9

Q9 Do you support the definition of Reportable Matters?

22. Yes.

Question 10

Q10 Do you believe that the proposals in ISA (UK) 2X0, considered collectively, will enhance and strengthen the auditor's identification of matters that should be reported to an appropriate authority outside the entity?

23. We cannot provide an answer to this question as we are not audit practitioners.

Question 11

Q11 Have appropriate enhancements been made to the application material?

24. We cannot answer this question as, not being auditors, we have not assessed the enhancements to the application material.

Question 12

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

25. Yes.

F. Concluding comments

26. If you wish to clarify any of our comments or discuss our thoughts further, please contact the signatory below.

Yours sincerely

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