



Quoted Companies Alliance

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The Quoted Companies Alliance is the independent membership organisation that champions the interests of small to mid-size quoted companies.

A company limited by guarantee registered in England
Registration Number: 4025281

AAT@frc.org.uk

Friday 14 June 2019

Dear Ms Dalby,

Exposure Draft: Proposed ISA (UK) 570 (Revised) - Going Concern

We welcome the opportunity to respond to the Financial Reporting Council's consultation on stronger Going Concern standard for auditors.

The Quoted Companies Alliance *Financial Reporting Expert Group* has examined the proposals and advised on this response from the viewpoint of small and mid-size quoted companies. A list of Expert Group members can be found in Appendix A.

Overall, we do not believe that the proposed revisions to International Standards of Auditing (ISA) (UK) 570 *Going Concern* will serve to enhance the quality and rigour of audit in relation to going concern.

In spite of the positive intentions, our principal concerns are twofold:

1. the proposed revisions do not promote a more robust process, and
2. they have fallen short of appropriately addressing the public interest.

In regards to the former, we are of the opinion that the additions in the revised standard will give rise to boilerplate auditing. This will not foster a deeper, more robust, analysis of the entity, its environment and the events and conditions that may cast doubt on the entity's ability to continue as a going concern.

As for the latter, and the extent that the public interest concern in light of recent corporate failures has been addressed, we believe that the revisions add only limited, or no, further value or clarity for users. As such, the expectation and knowledge gaps remain.

If you would like to discuss our response in more detail, we would be happy to attend a meeting.

Yours sincerely,

A handwritten signature in blue ink, appearing to read 'TW', with a horizontal line extending to the right.

Tim Ward
Chief Executive

Q1 Has ISA (UK) 570 been appropriately revised to promote a more consistent and robust process in respect of the auditor's responsibilities in the audit of financial statements relating to going concern going concern? If you do not consider this to be the case, please set out why?

Whilst the intention to revise ISA (UK) 570 may have been to make it a more consistent and robust process, it has, on the whole, failed to do so. Despite ISA (UK) 570 becoming more consistent with the likes of ISA 540 and ISA 315, it is unlikely to result in a more robust process for the reasons set out below.

Additionally, the FRC has missed the opportunity, within these proposed revisions to ISA (UK) 570, to clarify the auditor's responsibilities where the use of an alternative basis of accounting is appropriate. For instance, the FRC has failed to clarify the impact on the auditor's reporting requirements where an alternative basis of accounting has been applied and is deemed appropriate. Furthermore, the FRC continues to limit its focus of the revisions to one element. Whilst we agree this is important, the consequence of such an approach is that all other aspects pertaining to going concern and other types of entities are overlooked with the exception of the application of ISA (UK) 570 in the public sector.

Q2 Do you believe that the revisions appropriately address the public interest?

No – we do not believe that the revisions have appropriately addressed the public interest. Notwithstanding the intentions of the FRC, the 'expectation' and 'knowledge' gap between the responsibility of the auditor and that of the directors will remain. This is particularly so in respect of the viability of an entity and whether or not it is a going concern. Although the FRC asserts that there will not be an expansion of the auditor's responsibilities out of line with what directors are required to do under law and regulation in respect of going concern, there is a risk that these changes will be misunderstood by the users of the financial statements and the wider public. This will serve to widen the expectation gap further, rather than reduce it.

Other than the requirement to give a more explicit statement on whether material uncertainty exists, the additional reporting requirements also add no further clarity. As well as this, the statement on whether material uncertainty exists inadvertently serves to boiler plate another element of the auditor's report and adds no value to the understanding of users. In order to address the public interest need, there should be more detailed and specific wording in the auditor's report. However, it should only be aimed at those entities where the public interest is greatest, such as for listed entities and large private companies.

Moreover, whilst changes are expected to be made by the FRC in light of recent corporate failures, the FRC has applied a blanket approach to all entities, irrespective of size, nature and risk. The 'scalability' paragraphs give no clarity on this matter and the FRC have omitted any scalability in respect of the reporting requirements under ISA (UK) 570. At present, the amendments made only apply proportionality to specific areas. Further amendments need to be made in order to ensure that the FRC applies proportionality appropriately and reflects this throughout all of the amendments in the revised standard.

Q3 Will the revisions promote a more robust process for:

a) Obtaining an understanding of the entity and its environment, the applicable financial reporting framework and internal control relevant to going concern?

We do not believe that the revisions promote a more robust process in respect of obtaining an understanding of the entity and its environment, the applicable financial reporting framework and internal control relevant to going concern. The additions in the revised standard in respect of this will lead to a boiler plate audit approach

being adopted by auditors. It will effectively result in another checklist at the planning stage which adds little value other than to act as a prompt for auditors to consider. It will not however encourage auditors to alter their current approach when considering the events and conditions which cast significant doubt on an entity's ability to continue as a going concern. The auditor already has to consider the entity and its environment as part of their planning approach, which includes elements that would impact on going concern. Thus, the additions to the standard simply crystallise this requirement, but do so in such a way that it adds little to change the current auditing process which the FRC does not believe will address the public interest concern with the latest corporate failures.

In regard to paragraph 10-3, there has been no articulation of what the impact would be on the auditor's assessment and approach to the overall conclusion on the entity's system of internal control where the entity has failed to perform the expected assessment. As the FRC purport, the ISAs should not be viewed in isolation. However, the proposed amendments to ISA (UK) 570 do not appear to consider the consequential impact of those changes on the overall audit of the financial statements. The reference to this in the application guidance would be better placed in the body of the standard itself, given the importance of the issue.

b) Obtaining sufficient appropriate audit evidence in relation to the adequacy of management's assessment

The revision to ISA (UK) 570 promotes a greater work effort in respect of this. However, it is likely to lead to a boiler plate audit approach. It is however observed that the changes align closely to the revisions and requirements under ISA (UK) 540.

Q4 In making an assessment of going concern, the directors are required to consider a period of at least 12 months. In evaluating the directors' assessment should the auditor be required to consider a longer period, and if so what should it be?

We do not believe that the auditor should be required to consider a longer period in making an assessment of an entity's ability to continue as going concern beyond the 12 month period assessed by the directors. This belief is particularly resonant if the FRC wants to align the requirements of auditors with that of the directors. For this reason, the FRC should not expand the period of assessment further than that required by the directors, especially considering the new and expanded auditor reporting requirements. Making such a change would effectively make auditors responsible for the going concern assessment of the entity rather than the directors themselves. The auditor is responsible for evaluating whether the assessment of an entity's ability to continue as going concern is appropriate and adequate, rather than making decisions for the directors.

Q5 Is it sufficiently clear from the revisions to the standard that the auditor is required to first identify whether there are events or conditions that may cast significant doubt on the entity's ability to continue as a going concern before considering whether there are factors which may mitigate those events or conditions?

No – we do not believe that the revised standard is sufficiently clear, as, at present, the information is hidden within the application guidance. In order to make the requirements clearer, the FRC should be more explicit in the standard itself. Doing so will highlight this requirement and ensure that auditors follow the approach set out in ISA (UK) 570.

Q6 Do the proposals sufficiently support the appropriate exercise of professional scepticism throughout the risk assessment procedures, evaluation of management's assessment and evaluation of audit evidence obtained?

The proposals sufficiently support the appropriate exercise of professional scepticism only insofar as it mentions the expectation for auditors to apply professional scepticism. Rather than auditor's failing to apply professional scepticism, the main difficulty lies with the evidence of that application.

Q7 Do you agree with the proposals for auditors of all entities to provide an explanation of how the auditor evaluated management's assessment of going concern (including key observations) and to conclude on going concern in the auditor's report?

No – we fundamentally disagree with the proposal for auditors of all entities to provide an explanation of how the auditor evaluated management's assessment of going concern and to conclude on going concern in the auditor's report. The additional narrative reporting requirements included in the proposal should be focussed on public interest entities, listed entities, those who voluntarily (or are required) to apply the UK Corporate Governance Code and large private entities only. The nature and style needed in this new requirement fits with that included in ISA (UK) 701 when reporting on key audit matters.

Auditors who have experience of reporting on key audit matters are aware of the style and content typically required, and it is also aimed at reporting to those users of financial statements relating to companies of public interest. To apply the same reporting requirements to smaller entities is excessive and unnecessary. The users of such financial statements are limited, and, as such, it is not necessary to include such information that adds no further value.

Aside from the scalability and proportionality of these proposals on auditor reporting, the FRC need to ensure that they are consistently applying the reporting requirement of noting 'key observations' in the audit report. For key audit matters, this is only suggested for public interest entities (PIEs) whereas there is no such suggestion for non-PIE entities where key audit matters are reported. In terms of consistency in reporting, it would be unusual for the FRC to mandate the inclusion of key observations for going concern, but not do the same for key audit matters.

Q8 Are the requirements and application material sufficiently scalable, including the ability to apply ISA (UK) 570 (Revised) to the audits of entities with a wide range of sizes, complexities and circumstances?

We do not believe that the requirements are sufficiently scalable for the reasons set out above. In addition to this, it is unclear in both the standard and in the application guidance which elements are 'scalable'. The only reference to the applicable paragraphs are within the consultation document itself. For clarity purposes, and for the FRC to demonstrate its purported approach to proportionality, it should clearly identify each area that is scalable through the use of appropriate heading and sign posting.

Q9 Do you agree with the proposed effective date (aligned to the effective date of ISA (UK) 540 (Revised December 2018))?

Whilst the changes will have a significant impact on the resources and readiness of firms to ensure that requirements of the revised standard are met, we agree with the alignment of the date. It is better to have the same effective date for all revised standards, including the Ethical Standard and other ISAs, than a staggered effective date implementation.

Q10 Do you agree with the withdrawal of Bulletins 2008/1 and 2008/10 as set out in paragraph 1.20? Is there guidance in these Bulletins which has not been included in the revised standard which remains useful and should be included?

Whilst it is accepted that these standalone bulletins are likely to be out of date, consideration needs to be given to their relevance in regards to the impact of Brexit and Brexit-related uncertainty on going concern. The FRC must ensure that, if it removes useful bulletins, it replaces them with guidance documents of equal use and relevance.

Q11 What mechanisms should the FRC employ to ensure there is widespread awareness of the Director's responsibilities in respect of going concern?

The FRC can employ a range of mechanisms to ensure that there is widespread awareness of a Director's responsibilities in respect of going concern, they include:

- Enhancing the existing wording in the auditor's report on explaining the directors' responsibilities;
- Being vocal in its expectations and issuing guidance papers to assist directors in understanding their responsibilities; and
- Suggest that Sir Donald Brydon recommends there is legislative change to increase the responsibilities of directors in relation to going concern.

Appendix A

The Quoted Companies Alliance *Financial Reporting Expert Group*

Matthew Howells (Chair)	Smith & Williamson LLP
Rochelle Duffy (Deputy Chair)	PKF Littlejohn LLP
Edward Beale	Western Selection PLC
Matthew Brazier	Invesco Asset Management Limited
Ben Courts Elisa Noble	BDO LLP
Anna Hicks	Saffery Champness LLP
Mark Hodgkins	Trackwise Designs LLP
Clive Lovett	Bilby PLC
Laura Mott	Haysmacintyre
Claire Needham	KPMG LLP
Matthew Stallabross	Crowe UK LLP
Jon Wallis	Grant Thornton UK LLP
Peter Westaway	Deloitte LLP