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Dear Mr Babington

Providing Assurance on Client Assets to the Financial Conduct Authority

Mazars welcomes the opportunity to respond to the consultation document relating to the above proposed new assurance standard. We support the Financial Reporting Council's intention to introduce the new standard as an important step towards improving quality and accountability.

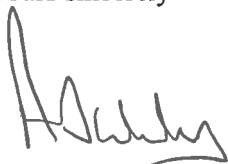
Our overview comments and responses to the specific questions raised in the consultation are attached.

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We appreciate our response is public and so may be quoted by other parties. We ask that any quote taken from our document is attributed to us, including that it is taken from this document; that it is used word for word and that it is not used out of context, its meaning changed through a partial extract or in any other way that would mislead.

If you would like to discuss our response with us please do not hesitate to contact me on 020 7063 4448.

Yours sincerely



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Providing Assurance on Client Assets to the FCA**OVERVIEW**

1. Mazars supports the Financial Reporting Council ('FRC')'s work in publishing the draft Standard in respect of providing assurance on Client Assets to the Financial Conduct Authority ('FCA') as an important step towards improving quality and accountability.
2. We accept that providing assurance in a direct reporting assignment involves considerable judgement on behalf of the auditor.
3. We consider the new standard as setting out the best practice already employed by CASS auditors, including documentation of custody asset and client money flows and the interaction between legal entity and rules and also risk assessment and evaluation of design control activities by the CASS auditor. However, the standard does not emphasise sufficiently the pivotal role and complexity of these aspects of the work and the commensurate specialist skills and time required to report on complex firms. We do not consider that for firms with simple operations and business models that this will be unduly onerous.
4. Our residual concern centres upon the use of the risk model and the judgements which are needed to determine a proportionate response. The key issue of proportionality arises from the potentially open ended nature of direct reporting of the effectiveness of the systems and controls operated by the firm ("the subject matter") against CASS rules ("the criteria"). Whilst the auditor will have regard to the work of the management of the firm, in essence the CASS auditor is as interested in what the firm does not do, but ought to, as much as in what it does.
5. We consider that the role of information technology and the specialist IT auditor is underplayed.
6. The extent of the bold paragraphs is such that without some additional guidance the standard risks having the look and feel of a CASS audit compliance check-list. We consider that there would be value in further discussion with practitioners.

RESPONSES TO FRC QUESTIONS**Q1: *Will the proposed Standard achieve its Objectives?***

Do you believe that the proposed Standard will meet the objectives set out in paragraph 19 of the Introduction and, in particular, improve the quality of client asset assurance engagements? If not, why not?

7. We believe that the standard goes a significant way to achieving its aims, but without guidance it risks a disproportionate response to manage risks within audit firms.
8. We think that the standard should emphasise "up-front" that the reasonable exercise of the professional judgement of the auditor required in direct reporting assurance assignments is what will determine whether the auditor has complied with the standard. The key aspects of this include a thorough and comprehensive evaluation and documentation of:
 - a. risk to CASS compliance and related decisions on determining the extent of work to be performed; and
 - b. the significance of findings and the rationale for the opinion.
9. This evaluation and documentation is essential in this standard to ensure that where an FCA supervisor takes a different view to the auditor, particularly during emerging practice such as regarding PS14/9 and perhaps eventually a further CP on CASS 5A, that the auditor is not unduly exposed.

Providing Assurance on Client Assets to the FCA

10. The FCA also requires s166 reviews in connection with CASS and these can have a wide remit in terms of end to end 'drains up' review of governance and oversight mechanisms in addition to considering systems and controls for compliance with CASS. The draft standard needs to make it clear that such a breadth of remit is not part of direct reporting upon CASS to avoid any misunderstanding.
11. Moreover, where a reasonable assurance review of compliance with CASS is included in a s166 or any other form of review then this should be in scope to avoid different standards for what is the same work.

Q2: Effective date

The proposed Standard is effective for reports to the FCA with respect to client assets covering periods commencing on or after 1 January 2016, with early adoption permitted. Do you believe that it would be appropriate to mandate the application of the Standard for earlier reporting periods to achieve the objectives set out in paragraph 19 for reporting periods commencing before 1 January 2016?

12. We consider that the standard codifies much of best practice and could be adopted early for some assignments.
13. It would not be appropriate to mandate an earlier start date if this is before the standard is issued. We prefer standards to be issued before their mandatory effective date.

Q3: Content of proposed Standard

The proposed Standard includes within a single document requirements relating to:

- a. Reasonable assurance engagements;
- b. Limited Assurance engagements;
- c. Special Reports; and
- d. Non statutory Client Money Trusts.

The FRC considered other possible approaches involving issuing a number of separate and shorter Standards. On balance, however, the FRC concluded that including all the requirements in a single document was likely to be the most helpful to practitioners and to mitigate the risk of practitioners, who perform relatively few engagements, from failing to select a relevant Standard to complete. Do you agree with including all requirements in a single Standard? If not, why not and what alternative structure for the Standards would you prefer?

14. We agree that including all the requirements in one document is the right solution. There are, otherwise, risks of failing to reference the correct material and of confusion arising from two or more documents embodying apparently different standards or approaches. Whilst some differences could be intentional and the risk minimised by careful drafting and sign posting, we think even subtle differences risk unacceptable confusion as to whether wider inferences should be made.
15. We support the approach of making very limited references to specific chapters of CASS for insurance intermediaries (CASS 5) and debt management firms (CASS 11), other than required for specific reports. This would be superfluous as the same underlying approach and standard of work should be applied whichever chapters and rules are applicable.

Providing Assurance on Client Assets to the FCA**Q4: Proportionality of requirements**

The proposed Client Asset Assurance Standard contains a combination of requirements (basic principles and essential procedures indicated by paragraphs in bold type) and guidance (application and other explanatory material). Do you consider the extent of the requirements to be proportionate to Client Asset Assurance Engagements which require the CASS auditor to make a direct report to the Financial Conduct Authority rather than reporting on an assertion by management? If not, why not? Please specify any requirements you believe to be unnecessary and any additional requirements that you believe should be included? In both cases please provide your reasoning.

Scope (11 and 108)

16. Proper scoping of the work is essential. Understanding how the asset and cash flows fall within the CASS rules and how the legal entities involved and their regulatory permissions interact with the rules is a key part of the work. There is a risk an inappropriate opinion will be issued if this understanding is incorrect.
17. This understanding, in combination with the work by the CASS auditor on risk assessment and design evaluation, is something which is best practice and would merit additional emphasis within the standard to reinforce the objective of ensuring the quality of CASS work.

Forming and managing the team (52 to 54) and IT

18. The only mention of specialists is in respect of "client asset specialists" (paragraph 52) and "specialist assurance responses" (paragraph 54). The only mention of information technology is in paragraph 55 in respect of IT change.
19. This is insufficient given the reliance upon IT by the client in most CASS engagements. For example, many systems rely upon the synchronisation of custody assets and client money, reliability of system interfaces and exchange of data with custodians. The use of IT specialists appropriately trained in the implications of their work for the work of the CASS auditor is essential.

Risk Model (67 to 79)

20. The risk model in paragraph 69 has four components. Only that relating to control risk is considered in depth in paragraph 72. The others receive limited attention and should be expanded to support the use of judgement in the extent of testing.
21. In particular, evaluation risk is included in paragraph 69d, but there is neither a link with the need to consult an internal or external expert nor EQCR as appropriate.
22. The list of evidence in paragraph 74 refers to compliance monitoring, but not internal audit. We think that the CASS auditor should also consider work performed by internal auditors. Many clients operate an integrated assurance model including three lines of defence.
23. This list of evidence in paragraph 74 and the draft standard does not consider legal advice supporting judgements made by management in their response to the potential risks of non-compliance with the CASS rules. In our view it is management's responsibility to obtain legal advice, for example, whether a firm is acting as a principal or agent or the scope of specific aspects of the Regulated Activities Order and exemptions. We consider that the auditor should not generally be expected to obtain such legal advice as part of a reasonable assurance engagement. Guidance is needed in the draft standard to ensure

Providing Assurance on Client Assets to the FCA

that auditors are only expected to take their own legal opinion in exceptional circumstance where, for example, they disagree with management.

24. Paragraph 77 references the need for the CASS auditor to perform its own risk assessment procedures. Whilst we agree the CASS auditor can have regard to management's assessment, the standard should make it clear that it cannot place uncritical reliance upon this in a direct reporting assignment and management's assessment should be evaluated with due professional scepticism. The draft standard should emphasise that this risk assessment by the auditor should drive its exercise of judgement as to the extent and focus of the testing as a key element of proportionality.

Response to Risk Assessment (80)

25. The draft standard should emphasise that the risk assessment by the auditor should drive its exercise of judgement as to the focus and extent of testing. We consider that proportionality means that some work must be performed in respect of each relevant rule, but the risk assessment may mean this is limited in nature in some areas with emphasis placed on other areas.

Evaluation of Design of Control Environment (81 to 93)

26. Paragraph 83 is potentially wide in its interpretation as to the extent of the evaluation of culture. The standard should make it clearer that this evaluation should be limited to consideration of the implications of evidence obtained during gaining the requisite understanding of the control environment. Otherwise there is a risk that the scope of the standard could be inadvertently extended to an end to end governance review which can form part of a s166 review, for example.

Testing Controls (97 to 98)

27. This offers little guidance on sampling in particular. The draft standard should consider the auditor's response when there is an elevated inherent risk e.g. arising from the firm's business model or as a result of failings in an aspect of CASS in a prior year.

Third Parties (108 to 112)

28. We consider that, dependent upon the evaluation of risk, the use of type II control reports to provide assurance evidence for the effectiveness of systems and controls relevant to the CASS auditor's opinion. Not to permit the use of such reports would entail the auditor visiting every third party supplier. This would be disproportionate and a potential mis-focus of work and threat to the overall quality of the assurance.
29. We would suggest that the standard provides some guidance on their use. It should consider whether all of the common frameworks such as ISAE 3202 and AAF 01/06 are acceptable.

Limited Assurance Engagements (146 to 160)

30. In paragraph 151 the use of exemptions is mooted. The standard should explicitly set out that it is disproportionate to test the firm's control over adherence to the exemption noting that it is not contemplated in the bold text paragraph in 153 to 160.
31. For complex situations the standard should make it clear that design of procedures alternative to those in 153 to 160 may be proportionate.

Providing Assurance on Client Assets to the FCA

32. We note that paragraphs 153 -160 fail to include the possibility of a review of bank statements and test of a sample of items by the CASS auditor. For many small firms with a simple business model operated at some distance from the actual flows of money and assets this is an appropriate and straight forward test.

Special reports & Internal System Evaluation Method ('ISEM') (168 to 175)

33. The sections on special reports offer the auditor little framework or guidance on the practicalities. For example:
- a. an insistence that the firm produce a comprehensive document of its own which can then be definitively referenced in the CASS auditor's opinion.
 - b. evaluation by the CASS auditor of scenarios of transactions and how they are dealt with by the control.
34. Whilst no report is needed on an ISEM, in principle the approach is similar. The auditor is still evaluating the design effectiveness of this and any guidance on special reports is relevant and should be referenced.

Non Statutory Trust (176 to 181)

35. The section correctly refers to the extension of the report to cover statutory trusts when a firm operates both these and non-statutory trusts (paragraph 179). We consider that paragraph 178 is unclear and should make it clear that the extension of systems and controls to both arrangements, in this context, means the firm must have control(s) to prevent the advancement of any credit.

Q5: Engagement Quality Control Review

The proposed Standard requires Engagement Quality Control Review to form an integral part of all reasonable assurance engagements. The FRC is of the view that the CASS engagement leader will typically be required to make a number of important judgments concerning the nature, extent and timing of assurance procedures and that the CASS engagement leader should be subject to engagement quality control review throughout the course of the engagement. Do you agree?

36. We appreciate that the definition of "Engagement Quality Control Review" (EQCR) in paragraph 10 contemplates that the person conducting an EQCR need not necessarily be a partner ("other person in the accounting firm"). However, we consider that guidance should be provided to make it clear that this person can be someone authorised by the firm's policies and procedures as there is risk that the requirement could be still interpreted as requiring that the reviewer should be a partner or responsible individual. This risks a disproportionate burden and moreover may exclude the use of appropriately experienced technical expertise from which authority for challenge springs.
37. We consider it disproportionate that there should be a mandatory EQCR of "all" CASS reasonable assurance engagements (paragraph 141 and 143) as this will impose an undue burden of process and documentation on firms with straightforward business models without significant impact upon quality. We think that criteria for an EQCR could be determined by the outcome of the risk assessment or the most significant CASS firms, noting that the FCA itself has categorised firms as small, medium and large. Using the FCA categorisation is superficially attractive, but the threshold of client monies of £1m for CASS medium firms would capture many general insurance intermediaries and that for custody assets of £10m would capture asset managers both of whom would have simple business models and for neither of which would EQCR be proportionate. However the threshold of £1bn and £100bn respectively for CASS large firms would potentially exclude

Providing Assurance on Client Assets to the FCA

firms which may be considered “in the public interest”. The FRC may need to establish an appropriate threshold or risk based criteria in consultation with practitioners and the FCA.

38. We do consider that all engagements should be subject to a form of second review but this may fall short of an EQCR and CASS auditors should be free to determine the nature of this. We would also emphasise that part of a proportionate response is the expectation of consultation internally for any engagement when a difficult judgement arises and for which the CASS engagement leader considers an additional review is needed.

Q6: Ethical requirements

The proposed Standard requires CASS auditors to comply with the FRC Ethical Standards for Auditors (concerning the integrity, objectivity and independence of the auditor) and the ethical pronouncements established by the CASS auditor's professional body. Do you agree with this proposal? Please provide your reasoning whether you agree or disagree with the proposal.

39. FRC Ethical Standards for Auditors specifically state that they apply to the audit of financial statements and, therefore, we consider that the only applicable ethical standards should be those of the auditor's professional body.

Q7: Requirements relating to training of CASS auditors

Paragraph 55 of the Contextual Material seeks to explain the implications for the training of CASS auditors of the mind-set required to complete CASS assurance engagements. The mind-set for performing a financial statement audit is different to the mind-set for performing a CASS engagement and, therefore, it may be dangerous to have audit staff perform a CASS engagement absent adequate training. The proposed Standard (see paragraph 36), therefore, includes explicit requirements for the CASS audit team to include staff who have received training in various aspects of CASS audits. Do you agree that the Standard should include requirements for staff training? If not, why not?

40. Relevant training for individuals in the CASS engagement team is critical.
41. The standard should make it clear that different requirements could pertain for a reasonable assurance and a limited assurance review and that the training shall be tailored to the complexity of the assignment(s). This is particularly due to the need to train for the evaluation of the design effectiveness of CASS systems and control and distinguishing this from other such work.

Q8: Communicating deficiencies in internal control to management and the governing body

In contrast to an auditor's report on financial statements a reasonable assurance CASS auditor's report is required (with some exceptions) to include a schedule of Rule Breaches. As a result of this requirement some contend that it is unnecessary for the CASS auditor to report deficiencies in internal control to both management of the firm and the firm's governing body both during the CASS audit and on its completion. The FRC, however, is of the view that matters may come to the CASS auditor's attention which whilst not being Rule Breaches per se are none the less of sufficient import to warrant reporting to both management and the firm's governing body. These requirements are set out in paragraphs 137 to 140 of the proposed Standard. Do you agree with the FRC's approach? If not, why not?

42. We agree with the FRC's approach.