

30 September 2019

Financial Reporting Council  
8<sup>th</sup> Floor  
125 London Wall  
London  
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Dear Sirs,

**RE: Exposure Drafts of the revised Ethical Standard and ISAs (UK)**

As users and preparers of financial statements, we have a significant interest in ensuring the integrity of financial reporting and recognise the important role played by the external auditor in this regard. We welcome the FRC's review of the Ethical Standard and ISAs (UK) and the continued efforts to enhance audit quality.

There have already been significant changes in the audit environment, which have seen a reduction in the volume of non-audit services provided by the audit firms to their audit clients. It continues to be a complex area, with different regulations limiting the services that may be provided by audit firms to their clients in different global locations. We believe that further clarity can be provided in this area in order to help reduce the risk of an unintentional breach of the independence requirements within the UK.

We note that the external auditor often has a unique understanding of a business, which means they are best placed to provide certain non-audit services. This is recognised in the existing demands from regulators and other third parties for the external auditor to provide extended audit or assurance in certain areas. We believe that the external auditor is best placed to provide these assurance services and that they do not directly impact on the auditors' independence, provided fees remain at appropriate levels. Although we support the inclusion of a list of permitted services and the additional clarity that this brings, we are concerned the current list of permitted services is too restrictive.

We believe that the provisions of extended audit or assurance services should not be restricted to engagements conducted under the same principal terms and conditions as the audit engagement and need not be limited to work that is integrated with the audit. In particular, we are concerned that the proposed ethical standard would restrict the external auditor from undertaking control assurance engagements where their unique knowledge means that they are best placed to undertake this work in an efficient and effective manner. In our opinion, restricting the provision of these and other similar assurance services is likely to increase the cost to businesses and reduce the overall service quality with no significant benefit in enhancing auditor independence. Our further responses to the exposure draft are attached.

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Equally important is the unintended consequence that the proposed changes may have of further reducing the number of firms able to bid on an audit tender. We already regularly hear from companies that getting firms who are both willing and able to bid for work is difficult. Many firms cite the level of non audit work as a reason why they are not submitting tenders. Further shifting the provision of non audit work away from the external auditor would in our view exacerbate this existing issue.

We continue to welcome appropriate action and challenge from regulators and other relevant bodies that enhances overall audit quality and we welcome further engagement on this subject.

Your faithfully

Richard Keers  
Chief Financial Officer

Jessica Ground  
Global Head of Stewardship

**Appendix A – Comments on Exposure Drafts of the revised Ethical Standard and ISAs (UK)**

Consultation question		Response
<b>Issues</b>		
1.	Do you agree with the revised definition of an 'objective, reasonable and informed third party' and with the additional guidance on the application of the test?	<p>The perspective of an 'objective, reasonable and informed third party', is a key concept in defining independence. In our opinion, revising the definition of this concept with one which has greater focus on the perspective of stakeholders better aligns the auditor's assessment of their independence with the expectations of key stakeholders including investors.</p> <p>We support the overall objective of this change and are pleased to see the inclusion of further application guidance, which seems clear and appropriate, and should assist firms in reaching conclusion that align with the expectations of stakeholders.</p>
2.	Do you agree with our proposed measures to enhance the authority of Ethics Partners, and do you believe this will lead to more ethical outcomes in the public interest?	<p>Overall audit quality is dependent on the overall conduct of the auditor. We believe that the enhanced role of the Ethics Partner will further help to promote a positive culture with high standards of ethical behaviour across the firms. We note that the success of this role is dependent on the effective implementation of wider processes and controls including appropriate training and internal review processes.</p>
3.	Will the restructured and simplified Ethical standard help practitioners understand requirement better and deliver a higher standard of compliance? If not, what further changes are required?	<p>We believe that the simplified Ethical Standard provides greater clarity as to the requirements and will help practitioners better understand their obligations as well as the expectations of stakeholders.</p>
4.	Do you agree with the introduction of a permitted list of services which the auditors of PIE audits can provide?	<p>As an investor and reporter we believe there is an opportunity to provide increased clarity as to permitted and non-permitted non-audit services. We therefore welcome the introduction of a permitted list of services that can be provided by the auditors of PIEs. However, we do not believe that further prohibiting the provision of non-audit services by statutory audit firms will necessarily contribute to an improvement in audit quality or result in a more cost efficient model.</p> <p>We are concerned that in some cases the further restrictions imposed by the list of permitted services may</p>

		<p>lead to less efficient audits, duplication of work and increased cost for shareholders with little or no perceived benefit. As an illustration of this point, control reports are often issued by companies to provide assurance to stakeholders as to the operating effectiveness of the company's controls as they relate to the provision of services to third party's. The controls tested often include controls that are also tested as part of an external audit. In some locations, control reports are also required by regulators (e.g. Switzerland). As the Ethical Standard is currently drafted, we believe these reports would be permitted where required by regulation but not permitted where required more generally as a result of market demands. We do not believe that these services gives rise to a perceived or actual threat to the auditors' independence and strongly believe that the external auditor is best positioned to deliver these services efficiently, avoiding duplicating, and effectively utilising their knowledge of the business.</p> <p>The issue above emphasises the importance of ensuring the drafting of the final ethical standard is clear. We believe the current drafting is open to interpretation as to when extended audit or assurance work (authorised by those charged with governance) would be considered "integrated with the audit work and..performed on the same principal terms and conditions". We do not believe that the Ethical Standard should prohibit the external auditor from providing extended audit or assurance on financial or performance information and/or controls where this is subject to a separate engagement letter.</p> <p>We note the drafting may also be open to interpretation as to whether a network firm can delegate the performance of certain services required by law or regulation to another network firm. We believe that it is important that a network firm is able to engage another network firm (including the audit firm) to perform parts of the engagement where that work is most efficiently provided by the audit firm. This is particularly important for global businesses where activities are often centralised. In these situations the network firm often rely on work perform by another network firm based where the relevant activities are being performed.</p>
5.	<p>Do you agree with the additional prohibitions we are proposing to introduce – in learning from the experience of enforcement cases</p>	<p>See response to question 4.</p>

	<p>like BHS, if the more stringent PIE provisions are to have a wider application to non-PIE entities, which entities should be subject to those requirements?</p>	
6.	<p>Do you agree with the removal of the reliefs for SMEs in Section 5 of the Standard, and the retention of reliefs for 'small' entities (in Section 6 of the Standard)?</p>	<p>No comment.</p>
7.	<p>Do you agree with the proposed removal of the derogation in the 2016 Ethical standard which allowed for the provision of certain non-audit services where these have no direct or inconsequential effect on the financial statements?</p>	<p>The audit is designed to meet the needs of shareholders. It is in the interest of shareholders that auditors are independent but also that the cost of non-audit services are not increasing with no added value.</p> <p>In our opinion it is extremely unlikely that the provision of certain non-audit services that have no direct or inconsequential effect on the financial statements would create an impence threat or lead to perceived or actual reduction in audit quality. We do not therefore believe the removal of this derogation to be necessary.</p>
8.	<p>Do you agree with the inclusion of FRC staff guidance within the application material, and has this improved clarity of the requirements?</p>	<p>We welcome the inclusion of any application guidance and believe this helps provide additional clarity.</p>
9.	<p>Do you agree with the inclusion of FRC staff guidance within the application</p>	<p>See response to question 8.</p>

	material of the auditing standards, and has this improved clarity of the requirements?	
10.	Do you agree with the changes we have made to ISAs (UK) 700, 250 A and 250 B, including the extension of the requirement for auditors to report on the extent to which their audits are capable of detecting irregularities, including fraud.	We believe clear and concise audit reports can improve the understanding of the assurance delivered from the audit process. We note that auditors reports are increasingly complex, whilst often containing generic information that does not assist users in fully understanding the business risks. We believe further emphasis should be placed on ensuring that the financial statements as a whole adequately identify the relevant risks to the business, including fraud, and also provide sufficient information to enable users to evaluate the material estimates and judgements applied by management.
11.	Do you agree with the proposed additional auditor reporting requirements, including the description of significant judgements in respect of Key Audit Matters and increased disclosure around materiality?	See 10 above.
12.	Do you agree with the revisions we have made to ISA (UK) 720, including the enhanced material setting out expectations of the auditor's work effort in respect of other information?	See 10 above.
13.	We are proposing changes to the standards to be	The effective date seems appropriate.

	<p>effective for the audit of periods commencing on or after 15 December 2019. Do you agree this is appropriate, or would you propose another effective date, and if so, why?</p>	
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