



# Association of Accounting Technicians (AAT) response to Financial Reporting Council (FRC) consultation on Revisions to Ethical and Auditing Standards 2019

## 1. Introduction

- 1.1. The Association of Accounting Technicians (AAT) is pleased to have the opportunity to respond to this consultation published on 15 July 2019.
- 1.2. AAT is submitting this response on behalf of its membership and for the wider public benefit of having a vibrant economy that encourages sustainable economic growth, technological development, social mobility and high levels of employment.
- 1.3. Although AAT is not a professional body for auditors, it does have an external audit exam and a significant number of its membership base work for audit firms. Additionally, AAT regularly responds to FRC consultations, is represented on the FRC's UK GAAP Technical Advisory Group and has FRC membership on its own Financial Reporting Panel.
- 1.4. AAT has not answered those questions which are not relevant to its members or where it does not believe it can add any value.

## 2. Executive summary

- 2.1. **Improving audit is imperative to improving the perception, standing and credibility of the wider accountancy sector.** It is important to note that whilst none of AAT's 140,000 members undertake audit work (although some may work for auditing firms), the consistent political, media and regulatory criticisms of the sector tarnish the wider accountancy sector, with many members of the public failing to distinguish between audit and the wider accountancy profession.
- 2.2. **Raising standards and ethics within the accountancy profession is a key objective for AAT as a professional membership body.** AAT has a charitable objective to advance public education and promote the study of the practice, theory and techniques of accountancy and the prevention of crime and promotion of the sound administration of the law.
- 2.3. **AAT agrees with the revised definitions, proposed measures to enhance the authority of Ethics Partners and simplification of the Ethical standard.** In fact, AAT supports almost all the proposed changes although it poses several questions to highlight challenges and/or uncertainty that may need additional attention.

## 3. AAT response to the consultation paper

### **Q1. 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?**

- 3.1. Yes. The definition provides reasonable clarity on the expected characteristics of the informed third party, and the additional guidance is helpful.

### **Q2. 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?**

- 3.2. AAT supports any efforts to promote ethics and therefore agrees with the proposed measures to enhance the authority of Ethics Partners.
- 3.3. AAT considers that the proposals are likely to further reinforce the importance of a consistent approach to the application of the Ethical Standard. However, where staff remuneration (including for board members, partners and the Ethics Partner themselves) is based solely upon financial factors, there will inevitably remain a conflict of interest. Additionally, other than an internal reporting mechanism, what protections will the Ethics Partner have if reporting potentially damaging or negative activity and behaviours in the context of the Ethical Standard?

**Q3. Will the restructured and simplified Ethical standard help practitioners understand requirements better and deliver a higher standard of compliance? If not, what further changes are required?**

- 3.4. The draft Standard appears to be clearly and logically structured and should therefore assist in practitioner understanding. However, the real test will be evidence, or otherwise, of long-term compliance levels.

**Q4. Do you agree with the introduction of a permitted list of services which the auditors of PIE audits can provide?**

- 3.5. AAT agrees with the introduction of a list of permitted services as this should provide greater certainty than a list of prohibited services.

**Q5. Do you agree with the additional prohibitions we are proposing to introduce – in learning from the experience of enforcement cases 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?**

- 3.6. The prohibitions are a positive step in terms of improving public trust. However, it may prove difficult to effectively define which non-PIE entities should be subject to the requirements without doing so on a case by case basis, which would probably not be feasible. This begs the question as to whether the provisions should be universally applicable except for 'small' entities.

**Q6. 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)?**

- 3.7. The same points apply as outlined in AAT's response to Q5, above. If the threats applicable to SMEs are such that their reliefs be removed, then that would appear to be appropriate. The alternative provisions and exemptions detailed at Section 6 of the standard would appear to be appropriate in ensuring that consideration of the ethical principles would be undertaken.

**Q7. 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?**

- 3.8. If, as suggested, this derogation was leading to unhelpful interpretations and this change will clarify the situation, then AAT agrees with the proposal.

**Q8. Do you agree with the changes we have made to Audit Regulation and Directive references within the ISAs (UK)?**

- 3.9. These proposed changes appear sensible.

**Q9. Do you agree with the inclusion of FRC staff guidance within the application material, and has this improved clarity?**

- 3.10. The inclusion of guidance is a sensible proposal as this will almost certainly aid clarity.

**Q10. 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?**

- 3.11. AAT strongly supports NOCLAR. AAT is very supportive of any actions that improve reporting and are likely to rebuild public confidence in audit and shine a light on any potential irregularities and fraud.

**Q11. Do you agree with the proposed additional auditor reporting requirements, including the description of significant judgements in respect of Key Audit matters, increased disclosure around materiality and disclosure of misstatements?**

- 3.12. The audit sector has often been slow to change and so AAT agrees that additional information requirements should be included within the auditing standards in order to ensure greater consistency and transparency in the market.
- 3.13. Requiring auditors to describe the significant judgements made in respect of how Key Audit Matters were addressed in the course of the audit is a far from onerous obligation and yet could provide crucial information and insight that could otherwise be lacking.
- 3.14. Likewise, clarifying what is meant by the term 'where relevant' as applied to the auditors of PIE entities when describing key observations arising in respect of significant risks of material misstatement is another sensible measure.
- 3.15. The need for enhanced disclosures in respect of materiality, including the specification of performance materiality, which shows the auditor's assessment as to the effectiveness of internal control in the entity is similarly another means of increasing transparency.
- 3.16. Finally, AAT supports Sir John Kingman's recommendation that a form of 'graduated findings' be introduced, where the auditor would be additionally required to give a view on management's decisions in areas that are key audit matters, including for example whether they were considered 'optimistic' or 'cautious'. This would be very helpful in clarifying auditors' genuine views as to the veracity of management decisions.
- 3.17. That said, AAT agrees that it would be prudent to wait until the conclusion of the Brydon review before making a final decision about whether to introduce this additional requirement.

**4. About AAT**

- 4.1. AAT is a professional accountancy body with approximately 50,000 full and fellow members and over 90,000 student and affiliate members worldwide. Of the full and fellow members, there are more than 4,250 licensed accountants who provide accountancy and taxation services to over 400,000 British businesses.
- 4.2. AAT is a registered charity whose objectives are to advance public education and promote the study of the practice, theory and techniques of accountancy and the prevention of crime and promotion of the sound administration of the law.

**5. Further information**

- 5.1. If you have any queries, require any further information or would like to discuss any of the above points in more detail, please contact Adam Williamson, AAT Head of Professional Standards.

