

December 2018

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# Post Implementation Review

## Providing Assurance on Client Assets to the Financial Conduct Authority

### Call for Feedback

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1. The FRC adopted a new standard on *Providing Assurance on Client Assets to the Financial Conduct Authority* in November 2015 (the Client Asset (CASS) Assurance Standard)<sup>1</sup>. The standard came into effect for periods commencing on or after 1 January 2016. When the standard was adopted, the FRC made a commitment to carry out a post implementation review of how well the standard had secured the objectives identified at the time of the consultation on adoption within three years.
2. The objectives we set for the standard are to:
  - Improve the quality of CASS audits and other CASS assurance engagements;
  - Adequately support and challenge CASS auditors when undertaking CASS assurance engagements and, in particular, to define the nature and extent of the work effort required for both reasonable assurance and limited assurance CASS assurance engagements without undermining the importance of the CASS auditor's judgment;
  - Support the objectives of the FCA's Client Asset Regime regarding the effective safekeeping of client assets and client monies and in particular to guard against systemic failure of the CASS Regime;
  - Manage the expectations of:
    - The management of firms that hold client assets; and
    - Third party administratorswhen a CASS auditor is engaged to provide assurance to the FCA on client assets that they handle or account for;
  - Support the effective training of CASS auditors by both the accounting bodies and other training organisations;
  - Help to establish realistic expectations regarding the integrity of the UK Client Asset regime with the beneficial owners of client assets; and
  - Underpin the effectiveness of the FRC's enforcement and disciplinary activities with respect to CASS assurance engagements.
3. The development of the standard was in response to some large and well-publicised failures in the audit of client assets and reflected significant work by the FCA to strengthen the CASS regime overall. It replaced audit guidance in the form of Bulletins with a series of mandatory requirements supported by application material. The standard also requires auditors to comply with the requirements of the FRC Ethical Standard and International Standard on Quality Control (UK) 1 (ISQC (UK) 1) when carrying out a client asset assurance engagement. This significantly strengthened the quality control and independence requirements around CASS engagements, which require the audit firm to ensure that it is competent to undertake a CASS engagement, including through having a thorough understanding of the standard.
4. Since the standard was adopted, two years of audits have been completed, for the years ending 31 December 2016 and 2017. We have met with stakeholders over that period, and with the FCA to discuss the results of those audits, and the impact that the standard has had both on audit quality, and on the readiness of entities who are subject to a CASS

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<sup>1</sup> <https://www.frc.org.uk/getattachment/3bf164e1-5158-4b2a-ade2-3070cf123e32/Standard-Providing-Assurance-on-Client-Assets-to-the-FCA-Nov-2015.pdf>

assurance engagement. We believe that the standard has had a positive impact on the quality of audit work undertaken, with evidence of significant investment by some audit firms in training to increase their dedicated CASS resources. The need for auditors to give an opinion both on the reported year end position, and on the efficacy of the control environment operated through the year being reported on, has also seen investment by audited entities to allow them to better prepare for audit by gathering and reconciling the information required and assembling evidence to demonstrate that controls have been working throughout the period.

5. Where stakeholders have challenged the standard, they have raised concerns about the increase in cost that they have experienced as a result of a more robust series of requirements for audit being in place. They have also asked how could those entities which are required to have a CASS audit, get greater value from the process, to help them further improve their control environment and procedures. Both auditors and audited entities have asked whether CASS engagements should apply materiality when developing their audit approach and reporting their findings to the Regulator.
6. In taking forward this Post Implementation Review, the FRC's principal concern is that the standard continues to support the FCA's objectives for the CASS regime in the UK. The standard was developed with the full support of the FCA, and we have sought the FCA's advice on how well their objectives are being met. Although it appears that the first year saw a higher number of modified reports, this number is now reducing. This is a welcome development, though we understand from feedback from the FCA that there is still more to do in terms of embedding the use of the new standard to build on this. The FCA advised us that: "*we are concerned that some audit firms have not invested sufficiently in building knowledge and understanding of our CASS rules and the FRC standard*" and the FCA has seen examples where auditors' reports failed to reflect significant deficiencies in CASS arrangements. We will ensure that in carrying out this post implementation review that we seek to identify ways to address this feedback, as well as reflecting any changes to the regime, since the standard was issued.
7. The FRC sets performance standards for audit and other public interest assurance engagements. CASS is clearly a public interest issue – those who own client assets need to have assurance that those assets are protected and can be returned to them with the minimum of delay should anything happen to a provider. High quality audit work, which provides assurance over the CASS regime operated by an entity is an important part of that assurance.
8. However, for statutory audit, the FRC is able to test the underlying quality of audit work undertaken. Currently we have no such powers in respect of CASS audits, and the FRC will only be able to examine a CASS audit in detail if it is referred for enforcement action, either following regulatory action by the FCA, or because there has been a reporting failing that has been referred to the FRC. We would be better able to test the underlying quality of work by establishing a monitoring regime whereby CASS work would be subject to FRC review. This post implementation review, therefore, seeks views on the desirability of a proportionate monitoring regime, which would follow the standard approach of the FRC's Audit Quality Review Team, would be based on reviewing a number of audits annually and underpin confidence in CASS audit work.
9. To support the Post Implementation Review, the FRC seeks feedback in respect of the questions set out in **Appendix 1**. Feedback should be sent by email to [AAT@frc.org.uk](mailto:AAT@frc.org.uk) and marked for the attention of **Mark Babington**. Feedback should be received by **5pm on Friday, 4 March 2019**.

## Appendix 1

### Feedback Questions:

- i. Do you agree that the CASS Standard has been successful in delivering the objectives set out in Paragraph 9 of the Introduction to the Standard and replicated in the covering paper? Please explain your reasoning.
- ii. Do you agree that the enhanced independence requirements of the FRC Ethical Standard have been positive in underpinning user confidence in CASS audit? Please explain your reasoning.
- iii. Do you believe that the quality of CASS audits has improved? If so what are the indicators of this?
- iv. Are there further steps that the FRC should consider including in the CASS Standard, to support the delivery of consistently high-quality CASS audits? Please set these out in your response.
- v. The standard requires the auditor to assess an entity's compliance with the FCA's CASS Rulebook. Are there any specific additional areas of guidance that should be developed to help in the assessment of whether custody relationships are fully compliant with the CASS Rulebook?
- vi. Bearing in mind that a primary objective of the standard is to support the delivery of the FCA's objectives for the CASS regime, including the safeguarding of assets held, and preventing failure of the regime, would you propose any changes to the current standard, and if so what would those changes be and why?
- vii. Do you believe that there would be benefits from bringing CASS audits within the FRC's audit inspection and monitoring approach? How do you believe any such monitoring scheme should operate?
- viii. Would you suggest any changes to the standard to increase the value of CASS audit to those entities that are subject to the regime? If so what changes would you propose and why?
- ix. Are there any other matters that the FRC should take account of in carrying out this post implementation review? If there are, please set them out in your response.

Respondents to this request for feedback do not need to respond to all of the questions.

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