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FAO: James Ferris
Financial Reporting Council

AAT@frc.org.uk

Dear Sirs

Consultation on Revisions to Ethical and Auditing Standards 2019

Kreston Reeves LLP appreciates the opportunity to respond to the consultation on Revisions to Ethical and Auditing Standards 2019, published by yourselves in July of this year.

Kreston Reeves LLP is a firm of Chartered Accountants that is amongst the top 25 largest firms in the United Kingdom. Based in London and the South East, we predominantly operate in the SME market providing audit and other accountancy services. Our client portfolio does though extend to include AIM-listed companies. We are a member firm of Kreston International, a global network of independent accounting firms. We are also a member of the Association of Practising Accountants and the Forum of Firms.

Our detailed responses to the questions raised in consultation are contained in Appendix 1.

Key points

The primary principle of ethical and auditing standards, and thus the proposed revisions, is to ensure that high quality audits are undertaken on a consistent basis across the profession. It should also be an objective to ensure that any changes made to standards are proportionate, and reflect the differing needs of PIEs and the wider market for audit services.

The perceived problems with audit quality that have resulted in considerable media attention and several recent reviews concerning the provision of audit services, in our opinion have arisen from the poor application of the existing requirements by certain auditors and should not necessarily be seen as a failure of the standards themselves. In general, we believe that high-quality audits can be achieved under the existing framework. Nevertheless, we believe that the proposed revisions will provide greater clarity and improve the quality of application.

If you have any questions on the contents of this letter then please contact Peter Manser at the address shown.

Yours faithfully

Kreston Reeves LLP

Appendix 1

Consultation on Revisions to Ethical and Auditing Standards 2019

Responses to specific questions

Question 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?

We agree with the revised definition and the additional guidance on the application of the test.

We would also welcome further practical guidance issued by the FRC on how to implement the test. This is a key part of the Standard, and is of particular importance at present with the high profile that certain auditors have following recent media attention. We feel that practical examples on how the test should be applied would be of considerable benefit to the profession by providing greater clarity on how to address common ethical issues faced by auditors.

Question 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?

We agree with the principal that the authority of Ethics Partners should be enhanced.

We suggest that the requirement to report to those charged with governance where an audit firm does not follow the Ethics Partner's advice, should be extended to all entities; not just PIEs as proposed.

We expect that the greater level of transparency created by these measures will lead to more ethical outcomes in the public interest.

Question 3

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?

We believe that the proposed measures will help practitioners understand requirements better and deliver a higher standard of compliance.

We would also welcome any additional clarity that the FRC can introduce to the standard through the greater use of clearer, understandable English and the avoidance of using confusing and hard to interpret terminology.

Question 4

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

We consider that a permitted list of services would provide greater clarity and less scope for interpretation than the current list of prohibited services. We therefore agree with this proposal.

Question 5

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?

We agree with the additional prohibitions proposed. We also agree that the more stringent PIE provisions should have wider application to non-PIE entities, to include 'Other entities of public interest' as defined in the proposed revised Glossary of Terms.

We do however, consider it essential that entities not meeting these definitions are not subjected to the same level of restrictions, which may prevent the provision of services to non-PIE SME clients in circumstances that we would consider to be inappropriate.

Question 6

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)?

We support the removal of the reliefs for SME listed entities in Section 5 of the Standard.

In our experience the Provisions Available for Audits of Small Entities set out in Section 6 of the Ethical Standard are rarely used in practice and in themselves are confusing. We see no need for the reliefs to be retained and should these provisions be withdrawn we consider that it would be unlikely that it would have any significant impact on the market for audit services.

Question 7

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?

We support the proposed removal of the derogation in the 2016 Ethical standard.

We would further support an outright prohibition of the provision of non-audit services to PIEs in order to demonstrate that the profession is taking seriously the public concerns that exist regarding the relationship between auditors and their PIE clients. Clearly this would not extend to services that it would be considered necessary for the auditor to undertake, usually as a consequence of statute.

Question 8

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

We agree with the changes made to Audit Regulation and Directive references within the ISAs (UK).

Question 9

Do you agree with the inclusion of FRC staff guidance within the application material of the auditing standards, and has this improved clarity of the requirements?

We agree with the inclusion of FRC staff guidance within the application material of the auditing standards. We believe that this has improved clarity of the requirements.

Question 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?

The 2016 revisions considerably enhanced the wording of the auditor's report to make clear what the auditor's responsibilities are. We support the proposed changes, which clarify the auditor's and management's respective responsibilities; particularly with regards to the prevention and detection of irregularities and fraudulent activity.

We would appreciate guidance from the FRC on how the changes to ISA (UK) 700 would be expected to impact audit reports for non-PIE entities.

Question 11

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?

We support the proposed additional auditor reporting requirements. We believe that these changes would help to narrow the 'expectation gap'. Unfortunately, some users currently do not fully appreciate what the scope of an audit is, and consequently have unrealistic expectations of what an audit should deliver.

Question 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?

Narrative reporting is an increasingly important part of the annual reporting process, yet the level of assurance that is provided is considerably weaker when compared to the financial statements. This is clearly an issue for legislation, which prescribes the level of assurance to be provided in order to meet the needs of users. Whilst we agree with the revisions made to ISA (UK) 720, we would like to see the narrative reports being given a status equivalent to the financial statements, and subject to similar, more robust audit requirements and removed from the financial statements so there is clarity on what has been subject to audit. Narrative reporting content not subject to audit could then be published on an entity's website.

Question 13

We are proposing changes to the standards to be 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?

We agree with the proposed effective date.