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Dear Mr Babington

Client Asset Assurance Standard

Grant Thornton UK LLP (Grant Thornton) welcomes the opportunity to comment on the Financial Reporting Council's (FRC) consultation 'Client Asset Assurance Standard'.

We set out in the Appendix A to this letter the detailed answers to the FRC's questions. Further, we have some detailed observations and comments on certain areas of the Standard which we have also set out in the Appendix B.

If you have any questions on our response, or wish us to amplify our comments, please contact me, Martyn Bellamy (tel: 020 7865 2466, email: martyn.bellamy@uk.gt.com) or Andrew Vials (tel: 020 7728 3199, email: andrew.vials@uk.gt.com).

Yours sincerely

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Responses to specific questions

Will the proposed Standard achieve its Objectives?

Question 1

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?

Response

We believe that the proposed standard will generally meet the objectives set out in paragraph 19 of the Introduction and improve the quality of client asset assurance engagements. We have the following comments in respect of certain objectives.

Objective (d): This objective will be met only if the management of the firms that hold client assets and third party administrators are aware of this Standard in advance of receiving the draft report from the CASS auditor. It is not clear as to how this awareness is to be achieved.

Objective (e): We believe that additional guidance is required in relation to the training of CASS auditors especially in respect of knowledge of trust and insolvency law.

Objective (f): As CASS audit reports are not publicly available for the beneficial owners of the client assets to review and assess, this objective will be met only if such owners are aware of the Standard and the CASS auditors report on client assets. It is not clear as to how this awareness is to be achieved.

Effective date

Question 2

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?

Response

We believe that it would not 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. This is because in our view sufficient time needs to be given to the firms to ensure the training is in place (as required by paragraph 36) and the CASS audit procedures undertaken by the CASS auditor have been amended to take account of any additional requirements stipulated by the Standard, once the final Standard is issued.

We believe that in the event the Standard is not finalised until after the end of Q1 2016, the effective date should be reconsidered.

Content of the proposed Standard

Question 3

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?

Response

We agree with including all requirements in a single document as it gives both firms and CASS auditors a single document for reference in respect of CASS engagements. Additionally, having all types of engagements in one single document enables firms to be aware of the implication that a change in permissions can have on them and the impact that will have on the CASS audit.

We note, however, that there is very little content relating to reasonable assurance engagements for insurance intermediaries holding client monies (CASS 5), including the effect of the £30,000 exemption limit. Likewise there is also little content relating to the Mandate rules (CASS 8) and the Collateral rules (CASS 3).

Proportionality of requirements

Question 4

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.

Response

We do not consider the extent of the requirements to be proportionate. This is because in our opinion some of the bold text requirements are more in the nature of guidance on how a particular requirement should be applied, and should not be mandatory.

We believe that further guidance should be given in the Standard on the level of work and procedures to be performed by the CASS auditor, especially in respect of limited assurance engagements. We recommend that this area is addressed to ensure consistency of work done by CASS auditors.

We expand on the proportionality and further guidance below.

Examples of the above are as follows:

- a) Paragraph 36 – This includes a 'for example' list for the training requirements and should therefore be guidance.
- b) Paragraphs 149 to 160 – Limited assurance engagements generally are easier to perform than reasonable assurance engagements. Accordingly, we are concerned as to the volume of bold text in paragraphs 149-160 and we believe that some of this could be presented either as guidance as to how the overarching objective could be achieved, or presented better as a bulleted list of matters that the CASS auditor is required to do.

It is likely that limited assurance engagements are particularly relevant to smaller firms where systems and controls may be less documented and formalised than would be found in larger firms. Accordingly, as there is a range of procedures that the CASS auditor could choose from to be able to obtain the limited assurance necessary to give the CASS report, the exact procedures should not be mandated. Therefore, we believe that the Standard needs to provide more guidance in terms of the nature and level of work to be performed by the CASS auditor on these engagements.

Additionally, paragraphs 151, 154 and 155 do not explain sufficiently the implications of finding control weaknesses in such engagements as the reporting on adequacy of systems and /or weak controls is outside the scope of the current wording requirement for a CASS limited assurance report.

- c) Paragraph 151 – This refers to evaluation of controls but if in a small firm the internal controls are weak or non-existent, there is no further guidance given as reporting on internal controls is outside the scope of the limited assurance opinion.
- d) Paragraph 154 – This paragraph refers to documentation of arrangements that the firm has in place to ensure that relevant staff members are aware of what constitutes client assets. If this documentation is not available in a small firm, the reporting of this deficiency is outside the scope of the limited assurance engagement. There is no further guidance given as to what the CASS auditor should do in these circumstances.
- e) Paragraph 160 – This rule is very specific for a Standard that covers a broad range of sectors and should therefore be guidance.

Engagement quality control review

Question 4

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?

Response

We agree that for reasonable assurance engagements the CASS engagement leader should be subject to engagement quality control review throughout the course of the engagement as this will provide an objective evaluation of the work done on a CASS engagement.

However, we have two reservations.

Firstly, we are of the view that the current wording in the Standard can be misleading (paragraph 141), as it refers to CASS reports being public interest engagements whereas in reality they are not available to the public. We suggest that the wording is amended as follows to reflect the importance of this work to the public:

As the effective segregation of client assets is of importance for public confidence a CASS auditor's system of engagement quality control shall encompass all such firm's engagements that provide reasonable assurance to the FCA on client assets.

Secondly, it is a bold type requirement but would be disproportionate if a firm only had one receipt of client money in a reporting period and would therefore trigger the Engagement Quality Control Review requirement. For example an insurance intermediary all of whose business, except for one client, is taken under risk transfer, and that one client does not meet the £30,000 exemption limit would be in scope.

Ethical requirements

Question 5

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.

Response

We do not understand the need to refer to the FRC Ethical Standards for Auditors in relation to the ethical requirements for CASS auditors because the matter is already covered by the FCA's Supervision Manual.

In this respect, we note that in the FCA's Supervision Manual, Guidance SUP 3.5.4, it is noted that *The appropriate regulator will regard an auditor as independent if his appointment or retention does not breach the ethical guidance in current issue from the auditor's recognised supervisory body on the appointment of an auditor in circumstances which could give rise to conflicts of interest.* The Code of Ethics for Professional Accountants (Section 291) has been derived from the International Ethics Standards Board of Accountants' (IESBA) Code of Ethics and therefore following The Code of Ethics for Professional Accountants (Section 291) would ensure compliance with the FCA's rules.

We suggest that the existing text in paragraph 24 is replaced with the following;

The FCA's Supervision Manual gives guidance in SUP 3.5.4 to the effect that "The appropriate regulator will regard an auditor as independent if his appointment or retention does not breach the ethical guidance in current issue from the auditor's recognised supervisory body on the appointment of an auditor in circumstances which could give rise to conflicts of interest". Accordingly, CASS auditors in the UK and Ireland are subject to ethical pronouncements established by the CASS auditor's recognised supervisory body.

Requirements relating to training of CASS auditors

Question 6

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?

Response

We agree that the Standard should include requirements for staff training as this will ensure that the CASS engagement team will have the required knowledge and experience to carry out the client asset work in compliance with the Standard and the Rules. Client asset reporting is specialist work that requires specialist knowledge and training. Training is also important on these engagements as the CASS report is a direct report to the FCA rather than on assertions made by management.

We believe that the second bullet point is too broad as it is not possible to give generic training around individual firm's specific business models. This information is given to the engagement team at planning stage rather than through generic training. We recommend this is reworded or explained more. In respect of bullet point four, it would also be helpful if the FRC indicates the sorts of problems it anticipates and comes across as it could prove difficult to provide training on the practical problems associated with review of reconciliations.

We believe that the Standard should also expand upon and clarify the extent of training required, especially when it refers to Trust and Insolvency law. An example of such guidance can be found within paragraphs 91 and 92 of FRC Bulletin 2011/2.

Communicating deficiencies in internal control to management and the governing body

Question 7

In contrast to an auditor's report on financial statements a reasonable assurance CASS auditor's reports 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?

Response

We agree that the internal control deficiencies that may come to the CASS auditor's attention during the client asset work should be communicated to management and the firm's governing body as they may give rise to reportable breaches of the CASS Rules in future periods.

However, we are of the view that the introductory paragraph 137 needs to be clearer. In particular, we suggest that the following sentence be added at the end of that paragraph, *Communicating deficiencies in internal control to management and the firm's governing body does not remove the requirement to report to the FCA, where appropriate, deficiencies affecting the adequacy of the firm's systems, notwithstanding that a rule has not been breached.*

Although the term *significant deficiencies* is defined in the draft Standard, we suggest that in paragraph 139 it should be clarified as to whether significant deficiencies are also breaches to be reported to the FCA. We make this suggestion because even if a deficiency has not resulted in a rule breach, the firm may not have maintained systems adequate to enable it to comply with the relevant CASS rules.

Furthermore, in paragraph 139 we believe that it would be helpful in understanding the requirement for reporting *on a timely basis* if it explained that this is to enable the firm's governing body to ensure that appropriate action is taken by management to resolve the deficiency, even while the CASS assurance engagement is in progress.

Detailed observations and comments

Where possible the observations and comments below follow the paragraph order in the draft Standard.

1) Introduction (page 3, paragraph 19 (d))

The wording in this paragraph refers to providing assurance to the FCA on client assets. In the case of insurance intermediaries, whilst the CASS audit report is addressed to the FCA, it is submitted to those charged with governance. We believe that it should be clarified here that in all cases except insurance intermediaries, the CASS audit report is sent by the CASS auditor directly to the FCA.

2) Contents (page 7)

From the contents page, it is not clear where the Standard's requirements are relating to the CASS 8 permission to control client assets. It is also not clear which specific sections relate to insurance intermediaries. We recommend that this is made clearer within the contents and the Standard.

3) Contents (page 8, Appendices)

We believe it would be helpful to CASS auditors of insurance intermediaries if there was an illustrative opinion related to those types of firm.

4) Definitions (pages 12, 13 and 14)

CASS audit: The definition of a CASS audit states that the client assets report is provided to the FCA. We recommend this definition is clarified to note that in the case of insurance intermediaries, the report is addressed to the FCA but submitted to those charged with governance.

Client Assets Report: We recommend the definition is amended to state that in the case of insurance intermediaries, the report is addressed to the FCA but submitted to those charged with governance as currently it states that report is required to be submitted to the FCA which is not true in the case of insurance intermediaries.

Limited assurance client asset report and Reasonable assurance client asset report: These definitions are difficult to comprehend. Whilst they appear to be based on the IAASB definitions, we recommend they are reviewed to ensure that they are readily understandable by the users of the Standard.

Walkthrough test: The definition is very broad where it suggests tracing a 'few' transactions. We recommend that guidance is given in respect of what is acceptable in this case. We also question whether this definition is meant also to encompass the walk through procedures referred to in paragraph 180 (c) of the draft Standard, where there should be no transactions to test, unless test transactions are run.

5) Establishing the firm's scope of permissions (page 15, paragraphs 12 and 13)

Two different words have been used in paragraphs 12 and 13 for the same person; *responsible individuals* and *responsible officials*. We recommend that, because the term *responsible individuals* has a specific meaning for audit firms, the word *responsible officials* should be used in both places.

6) **Opinions in reasonable assurance reports (page 15, paragraph 14)**

This paragraph refers to firms that have the permission to hold or control client assets. We recommend that it should be clarified that a reasonable assurance report is not required if a firm can only control but not hold client assets.

7) **Opinions in reasonable assurance reports (page 15, paragraph 15) and Inherent risk and control risk (page 25, paragraph 76)**

Paragraph 15 implies that the CASS auditor is responsible for reviewing the accuracy of the CMAR, whereas this falls outside the scope of a CASS audit or CASS reporting. We suggest that the Standard should clarify exactly what is the responsibility of the CASS auditor in respect of review of the CMAR and the extent of work to be carried out by the CASS auditor.

This applies also to paragraph 76, where we believe that the level of work to be done on the CMAR submissions needs to be clarified. Also, it needs to be clarified whether there any reporting requirements in relation to inconsistencies found by the CASS auditor in respect of the CMAR review.

8) **The client asset report (page 18, paragraph 32)**

We believe that paragraph 32 should be guidance rather than a rule because it is not about work the CASS auditor does to reach a CASS audit opinion, rather it is about the administration of the engagement, in this case timing. We recommend that the wording is amended as follows:

In order to facilitate the processes outlined in the two preceding paragraphs the CASS auditor should consider discussing with the firm what constitutes "an adequate period of time" and recording the agreement with the firm.

9) **Professional scepticism, professional judgement, and requisite mind-sets (pages 19 and 20, paragraphs 39 and 40)**

We agree that the first sentence of paragraph 39 should be bold text. However, the rest of paragraph 39 should be guidance explaining professional scepticism.

We believe paragraph 40 should be guidance and should be reworded as:

Professional scepticism is used in assessing the plausibility of information and explanations provided to it by the firm's governing body and management. Where appropriate the engagement team considers this in the context of their knowledge and their findings derived from other areas of work undertaken with the same firm.

10) **Compliance and insolvency mind-sets (page 20, paragraph 42)**

We recommend that the term *insolvency mind-set* should be explained in the Standard so as to provide clarity to the CASS auditor, especially as it is part of the mandatory training of the team.

11) **Documentation (page 21, paragraph 49)**

We recommend that the Standard clarifies whether the retention period is that normally used by a firm for its working papers or whether a different specific period is required.

12) **The CASS auditor's duty to report to the FCA (page 22, paragraphs 58 and 61)**

The term *breaches of the FCA's Rules* should be expanded to clarify that it is any breach not just CASS breaches.

- 13) **The CASS auditor's right to report to the FCA (page 23, paragraph 65)**
We believe that the word *directors* in two places in this paragraph should be replaced with *those charged with governance* as Partnerships do not have directors. Additionally, we suggest that an indication is given as to what is a *reasonable period of time*.
- 14) **Inherent risk and control risk (page 25, paragraph 74)**
We believe that the examples of other sources of information (given in bullets) should be guidance rather than a rule, as the rule is noted in the first sentence of paragraph 74.
- 15) **Determine the nature and extent of risk assessment procedures (page 27, paragraph 85)**
We believe that some guidance would be useful in terms of what the implications are and what the CASS auditors should do where, in the case of small firms, the risk assessment process is not formalised and/or documented. Failure to identify a risk is not in itself a problem if controls are designed and implemented such that the relevant system is adequate.
- 16) **Selecting items for testing to obtain evidence of operation of controls (page 29, paragraph 98)**
Point (a) of paragraph 98 refers to a *small number of items*. We think this calls into question what is meant by 'small'. We recommend that the wording be amended by replacing *is a small number of* with the words *are a few*.
- 17) **Forming client asset opinions (page 32, paragraph 118)**
We suggest that it should be made clear that the CASS auditor is required to report *all breaches of the relevant CASS rules*, not *all breaches*, particularly as the breaches register would include also non-CASS breaches.
- 18) **Content of a reasonable assurance client asset report (page 34, paragraph 129)**
Points (d) and (e) of paragraph 129 refer to nominee companies and secondary pooling events. As the reporting requirements for these are different from those for the custody rules, the collateral rules, the mandate rules and the client money rules, and are linked to adequate systems and period end, we recommend that reference to them be deleted in those points.

Two new points should then be added to the list after point (e).

The first of these is:

Where required by SUP 3.10.5R(3), an expression of opinion as to whether the firm's nominee companies that are subsidiaries of the firm, and in whose name custody assets are registered, have maintained throughout the period systems for the custody, identification and control of custody assets which a) were adequate; and b) included reconciliations at appropriate intervals between the records maintained (whether by the firm or the nominee company) and statements or confirmations from custodians or from the person who maintained the record of legal entitlement.

The second is:

Where required by SUP 3.10.5R(4), a statement as to whether the firm has complied with the rules in CASS 5.6 and CASS 7A (Client money distribution) and CASS 11.13 (debt management client money distribution rules) in relation to that pooling event.

19) Circumstances giving rise to limited assurance opinions (page 37, paragraph 148)

While we agree with the analysis of the requirement in SUP 3.1.1R, we believe that guidance is required in respect of the last sentence of this paragraph where it states that the auditor under CA 2006 is responsible for submitting a client asset report to the FCA notwithstanding that they may not have been formally appointed as a CASS auditor.

There are two reasons for this:

- (i) to be the CASS auditor there needs to be an engagement letter for the specific appointment (paragraph 25 (c) of the draft Standard)
- (ii) we believe that the auditor cannot provide a CASS report to the FCA if someone else is appointed as the CASS auditor (ie a firm can have only one CASS auditor at a time).

20) Limited assurance client asset reports (pages 37-38, paragraphs 149-160)

Limited assurance engagements generally are easier to perform than reasonable assurance engagements. Accordingly, we are concerned as to the volume of bold text in paragraphs 149-160 and we believe that some of this could be presented either as guidance, or presented better as a bulleted list of matters that the CASS auditor is required to do.

We believe that the Standard needs to provide more guidance in terms of the nature and level of work to be performed by the CASS auditor on these engagements, keeping in mind smaller firms where the controls may not be well documented and formalised.

21) Limited assurance client asset reports (page 37, paragraph 151)

We suggest that additional guidance needs to be given in terms of the extent of the procedure to be performed by the CASS auditor to establish the eligibility of the firm to exemptions from the CASS rules.

22) Requirements applicable to the provision of reasonable assurance with respect to special reports (pages 42 and 43, paragraph 175)

Is the reporting to the FCA in the circumstances noted to be under the 'whistleblowing' requirement or CASS report, or both? We suggest this is clarified to indicate that an ad hoc report to the FCA is also required.

23) Requirements applicable to CASS auditor confirmations in connection with non-statutory client money trusts (page 44, paragraph 180)

Paragraph 180(c) notes that the CASS auditor should perform on a sample basis walkthrough procedures to establish whether controls have been put into place as designed. This is not possible as it is clearly stated in paragraph 178 that a firm may not handle client money through a non-statutory trust unless it has the adequate systems and controls, and CASS 5.4.4R(2) requires the auditor to report before client money is placed in a non-statutory client money trust account; therefore there will be nothing to sample. Accordingly, we suggest that paragraph 180(c) should be deleted.

24) Requirements applicable to CASS auditor confirmations in connection with non-statutory client money trusts (page 44, paragraph 181)

Paragraph 181(a) notes that the CASS auditor shall meet with the designated manager and discuss the manager's authority, scope of work and findings. The requirement for discussing the *findings* with the designated manager is not included in CASS rule 5.4.4; in particular, the designated manager only has to *oversee*, so this needs to be clarified in

terms of what *findings* mean given that the designated manager does not have to have *findings* and also as to whether it should be part of the Standard.

25) Contextual material to the client asset assurance standard (page 65, paragraph 3)

Background

This paragraph notes that the CASS auditor is responsible for submitting a client assets report to the FCA but this is not true in the case of insurance intermediaries where the report is submitted to those charged with governance rather than to the FCA. We suggest that this should be clarified.

26) Contextual material to the client asset assurance standard (page 67, paragraph 9)

Four fundamental principles

We suggest that in the identification paragraph it needs to be emphasised that the identification of client assets needs to be at a legal entity level rather than at a business level where there could be multiple entities within a business division. This is important for reporting at a legal entity level.