

**Minutes of a meeting of the Audit and Assurance Council of the FRC  
held on 27 September 2017 at the FRC, 8<sup>th</sup> Floor, 125 London Wall, London, EC2Y 5AS**

**PRESENT**

Sue Harris	Chair
Olivier Beroud	Member (from Minute 1 to 10.5)
Mary Cleary	Member
Bryan Foss	Member
Jane Fuller	Member (from Minute 1 to 10.6)
Scott Knight	Member
Stephen Oxley	Member
Jerry Wedge	Member (from Minute 1 to 7.9)

**OBSERVERS**

Shelagh McAlpine (IAASA)  
Michael Gaull (PRA)

**IN ATTENDANCE**

Kate Acott	Project Director
Mark Babington	Deputy Director of Audit Policy
Anu Bhartiya	Committee Secretary
Keith Billing	Project Director
James Ferris	Project Director
Josephine Jackson	Technical Director
Melanie McLaren	Executive Director of Audit and Actuarial Regulation

**1 Welcome and apologies**

The Chairman welcomed everyone to the meeting and in particular Mary Cleary and Shelagh McAlpine (IAASA Observer) to their first meeting. Apologies were noted from Kari Hale (Council Member), Lee Piller (FCA Observer) and Marek Grabowski (Director of Audit Policy).

**2 Declaration of conflict of interest**

There were none reported.

**3 Minutes and Rolling Actions**

*Minutes*

- 3.1 The minutes of the Audit & Assurance Council meeting held on 12 June 2017 were approved for publication.

*Rolling actions*

- 3.2 The matters arising log which included rolling actions from previous meetings was noted.
- 3.3 The matters arising log for the Council Away Day held on 13 July 2017 was also noted. The Council's advice to the Codes & Standards Committee, given at the away day, to withdraw PN 25 – Attendance at Stocktaking was formally noted and minuted.

#### **4 Chair's update**

4.1 The Chair reported that the Codes & Standards Committee had met twice since the last Audit & Assurance Council meeting and amongst other matters had:

*21 June 2017*

- Discussed the Developments in Audit Report 2016-17.
- Recommended to the Board the approval of the revised ISAs (UK) 250, 330 and 505 and the Consultation on new Anti-Money Laundering guidance and approved the withdrawal of Bulletins 2007/02, 2011/01 and Practice Note 27.
- Received an update on Corporate Governance Code & Strategic Guidance Review.
- Approved the Triennial Review 2017 Feedback Statement on Approach to changes in IFRS, recommended to the FRC Board that it approved the issue of the Amendments to FRS 101 and the associated impact assessment and feedback statement to FRS 101 Reduced Disclosure Framework, noted the annual review of SORPS and approved FRED 68 Draft amendments to FRS 102 – Gift aid payments by subsidiaries to their charitable parents for consultation.

*12 September 2017*

- Discussed the consultation on Corporate Governance Revised Code.
- Discussed the Annual Review 2016-17.
- Received an update on Financial Reporting Lab activities.
- Received an update on Horizon scanning – Block Chain.

4.2 Melanie McLaren (MM) reported that the Board had met twice since the last Audit & Assurance Council meeting and amongst other matters had:

*5 July 2017*

- Approved the FRC Annual Report & Accounts for the year ending 31 March 2017.
- Confirmed that FRC had fulfilled its Competent Authority for Audit responsibilities.
- Provided approval for the final report on the '2016/17 Developments in Audit' which was issued in July 2017.

*13 September 2017*

- Discussed the FRC's next 3 year strategy which would mainly focus on corporate governance, what would happen post-Brexit and on making corporate reporting relevant to all stakeholders. This would also set out plans to build on the success of taking on the role of Competent Authority to build stronger trust in the assurance to investors from the audit process, grounded in high quality audit and a well understood framework of professional standards. We will also need to be aware of the implications of a background of rapid technological change for companies and for auditors.

4.3 MM informed the Council how the FRC is continuing to maintain and develop strong bilateral relationships with EU and other member state regulators, and how the international influencing strategy might need to develop during the Brexit transition period. The Council discussed how audit firms are thinking about managing the potential consequences of Brexit on the mobility of qualified staff, noting that there was participation by audit firms and professional bodies in the FRC's Brexit Stakeholder Forum.

4.4 Following a query in respect of *Going Concern*, Mark Babington (MB) informed Council that the matter would be included in the agenda for the October meeting. The project will include the review of all guidance material much of which was developed and issued in response to the financial crisis to ensure that it remains fit for purpose, and

that, where possible, material should be consolidated within the standard (ISA (UK) 570) itself.

## **5 Report of the Director of Audit Policy**

- 5.1 MB provided an update to the Council on the meeting with the FCA and ICAEW CASS Working Group which had discussed feedback on the first year of CASS audits using the new FRC CASS standard. The Council noted that the feedback has been positive and that regulated entities have undertaken significant work to better explain, document and evaluate their CASS control systems. The Council suggested that it would be useful if FCA could provide more information on how many of the qualified reports of regulated entities had material CASS breaches and if there were any wider implications to consider from the perspective of the Standard. MB reported that the CASS standard is unique in that for reporting breaches, it has no materiality threshold. Since the standard came in force from 1 January 2016, the regulated entities continue to strengthen their control systems, and in so doing make themselves better prepared for audit.
- 5.2 It was reported that Data Analytics would be included in the agenda for the November meeting.
- 5.3 The Council considered the ICAEW's letter in respect of Practice Note 21, which had raised some major flaws. The Council provided its advice in support of the FRC's proposal that PN 21 be withdrawn, and that any necessary matters would be addressed when PN 19 is updated in 2018. It was noted that PN 19 would be updated when the IAASB finalise ISA 540.
- 5.4 Following a request, MB informed that the list of all practice notes and bulletins issued by the FRC and when they were last updated was available on the website. He agreed to email the list to all Members for information.
- 5.5 The Council noted that once the FRC had consulted on revisions to the UK Corporate Governance Code, revisions would be made to a number of legacy bulletins – this will mean that most of the back catalogue will have been updated.
- 5.6 MB informed that the first workshop with Audit Firm INEs on the 'value of audit' had taken place. A further discussion with the INE working group is planned for October and the Council will receive feedback at a future meeting.

## **6. IAASB Update – Quality Control Project**

- 6.1 Josephine Jackson (JJ) provided a high level update on the IAASB's proposals for the quality control standards in respect of the firm's system of quality control and how it could be enhanced at the engagement level and for networks. The Council noted the project timetable which included the phases of exposure drafts and publication of a final standard.
- 6.2 With the revision of the ISAs, the Council queried the scale of change required in technology and methodology in audit firms. It was reported that the change would be positive and would depend upon the size and network of firms.
- 6.3 In terms of timelines, it was reported that the working draft of the revised ISQCs will be presented to Council in March 2018 and the Exposure Draft when issued in September 2018.

## **7 AAT Project Update**

### *Preliminary Announcements*

- 7.1 James Ferris (JF) provided a high level summary of the responses received in respect of the Discussion Paper on *Auditors and Preliminary Announcements*. The Council considered the Feedback Statement and Impact Assessment and noted that the majority of the respondents showed little appetite for any significant change to auditors' responsibilities as currently set out in the existing Bulletin. Through discussion, a number of comments and observations were made including:
- The respondents feel that any requirement on auditors requiring them to complete the audit of statutory financial statements and sign the audit report before agreeing the publication of preliminary announcements would disrupt and delay the process. There was, therefore, support to maintain the status quo, although there was scope for auditors to provide additional voluntary reports setting out for stakeholders the status of their audit work.
  - Inconsistencies between the preliminary announcements and audited financial statements are extremely rare. However, companies are required to provide reconciliation as required by the FCA/UK Listing Authority.
  - The existing Bulletin will be revised in coordination with the FRC's Corporate Reporting Team which is concluding its work on the format and structure of preliminary announcements in liaison with the UK Listing Authority.
  - With regards to the proposal of making the material included within the preliminary statements as 'Fair, Balanced and Understandable', a great majority of the respondents opposed the proposal as it would be difficult to meet this requirement in absence of explicit obligation being placed on company directors by the FCA / Listing Authority.
- 7.2 A member asked whether there would be any merit in reviewing the scope of Alternative Performance Measures (APM), which is work being undertaken by the Corporate Reporting Review Team who are looking at the guidance provided by ESMA, and who are undertaking a thematic review. Council requested an update on the Corporate Reporting Review Team's work on the developments in APM be provided to Council at a future meeting.
- 7.3 The Council provided its advice in support of the draft Feedback Statement, and that changes be proposed to the Codes & Standards Committee for approval.

### *PN 15 – The Audit of Occupational Pension Schemes in the UK*

- 7.4 Keith Billing (KB) provided a high level feedback on the responses received to the Consultation of the revision of Practice Note 15 *The Audit of Occupational Pension Schemes in the United Kingdom*. The Council considered the Feedback Statement and Impact Assessment and noted that there was overall support for the FRC's objective in revising the guidance. However, certain respondents identified some matters where more clarity in guidance would be helpful. The FRC's position was not to provide guidance other than to assist with the application of the ISAs (UK). As a result, the FRC was minded not to expand the guidance in the draft, or change the position previously discussed with Council on Going Concern. The draft has, however, been amended to make clear what matters may be judged to represent a material breach of the schedule of contributions or payment schedule.
- 7.5 A Member queried if any pension trustees were involved in the process of revising the Practice Note. It was reported that work was developed with the assistance of an expert working group that included representation from audit firms, the pension industry and the Pension Regulator. It was agreed that view of pension trustees appointed on the Actuarial Council would be obtained as an additional measure. *It was*

since confirmed that Trustees had been represented throughout the process, and therefore further review would not be needed.

- 7.6 The Council noted that in revising PN 15, it is proposed to withdraw PN 22 *The Auditor's Consideration of FRS 17 'Retirement Benefits' Defined Benefits Schemes* which is superseded by material in the revised ISAs. The Council agreed that its advice be provided to the Codes and Standards Committee that it approve for publication the revised PN 15 along with the Feedback Statement and approve the withdrawal of PN 22.

*PN 11 – The Audit of Charities in the UK*

- 7.7 Kate Acott (KA) provided a summary of the feedback of the responses received to the Consultation of the revision of Practice Note 11 – *The audit of charities in the United Kingdom*. The Council considered the Feedback Statement and Impact Assessment and noted that there was overall support for the FRC's objective in revising the Practice Note. KA highlighted that many of the respondents had given helpful editorial suggestions. Some suggestions did not represent widely held concerns and therefore the FRC does not believe that significant new guidance should be added in respect of them. Through discussion, a number of points and observations were made including:

- A respondent disagreed with the guidance in the PN on ISA (UK) 720, arguing that the trustees' report for charities that are not companies does not meet the definition of 'statutory other information' (SOI). However, both company and charity legislation include requirements for the auditor to report on other information in the trustees' report and therefore it does meet the definition of SOI.
- Some stakeholder bodies had expressed concern in respect of inconsistent practices between auditors regarding the communication with the trustees about disclosing related parties and related party transactions. It has been clarified in the guidance that the auditor shall obtain written representations from management and, where appropriate, those charged with governance. In addition, the auditor may choose to request individual confirmations from each individual trustee where considered necessary.
- The section on Reporting matters of material significance to the charity regulators has been updated for the recent publication of new guidance from the UK Charity Regulators.

- 7.8 It was clarified that the PN was not to guide trustees with their responsibilities but to assist auditors in the application of auditing standards in a proportionate way to the audit of financial statements of charities, thereby supporting high quality audit. The Council agreed that its advice be provided to the Codes and Standards Committee that it approve for publication the revised PN 11 along with the Feedback Statement.

## **8 Audit Quality Feedback**

- 8.1 MB briefly introduced the paper and noted that the ACCIF's feedback on the Audit Quality Practice Aid was positive, therefore there is no proposal to update the Practice Aid at this stage. However, going forward it would be reviewed in light of the outcomes of the consultation on the revised Corporate Governance Code and ISA 540. This review would be included in the forward planner for 2018 Q3/Q4. The review would also take into consideration ways for wider engagement with audit committee chairs and how the FRC can support better discussion around how high quality audit can be delivered.

- 8.2 The Council considered the feedback received from the audit quality survey of audit committee chairs. Through discussion, a number of points and suggestions were made including:

- There had been an encouraging level of participation with more granular responses to the revised format of the survey.
- Arising from the bilateral engagements with the Audit Committee chairs and the comments and themes emerging from the survey, proposals would be presented to the ExCo on how to structure future surveys, as part of a wider strategy for engagement with audit committee chairs and members.
- With regards to the concern relating to boiler plate reporting, FRC will be offering advice to the Investment Association, on how they might encourage further innovation in reporting through their 2018 extended auditor reporting awards.
- The outcome of the survey has been communicated to the participants through the Developments in Audit Report 2016-17.

8.3 It was agreed that the Council Members would send their comments, if any, on the survey to MB by email. MB agreed to summarise the key themes emerging from the survey for the next meeting.

## **9 FRC Audit Policy Questions**

9.1 MB highlighted three policy issues that emerge either from consultations that the FRC is currently responding to, or from the work that AQR Team is undertaking. These issues may need clarification for their application in the UK audit market.

### *ESMA consultation on the European Single Electronic Format (ESEF)*

9.2 The Council discussed the ESEF requirement coming into force from 2020 which will require each annual report to be tagged using XBRL and validation from the statutory auditor or the audit firm as to whether they have been correctly tagged. This would require an auditor to provide either an opinion or an assurance conclusion which may involve significant judgement. The Council also discussed the requirement for the true and fair view opinion to apply only to the machine readable version of the annual report, rather than both the human readable and the tagged version and how an auditor would be able to validate the consistency of both versions of the report. Subject to how this issue is addressed in the law, as a result of the outcome of Brexit negotiations, consideration would need to be given as to how to address this requirement, should it become an integral part of a statutory audit.

9.3 It was reported that going forward, further updates on this matter would be provided through the Report of the Director of Audit Policy.

### *Retention of data*

9.4 The Council discussed the expectations of firms about the period that they should retain data sets they use for audit purposes or whether it is possible for them to just retain the script they have used to run their analytical review. The discussion involved whether it would be pragmatic to require firms to retain data for two audit cycles whilst also considering the implementation of GDPR and the data protection requirements. Council Members discussed the implication of retaining 2 years data by a large audit firm and felt that it might not be pragmatic due to large quantity of data. The discussion included how other audit regulators are dealing with this issue, and noted in the US there is no requirement to retain the data set on file.

9.5 Consideration was given to the requirements of data retention and audit working papers as set out in ISQC and the ISAs. The Council suggested that consideration should also be given to the requirements of the Enforcement and the AQR Team when an audit trail is performed.

- 9.6 MB informed that a further update on this matter will be presented to the Council at a future meeting.

*Application of materiality*

- 9.7 MB informed that there appear to be inconsistencies between how certain audit firms have considered materiality when designating a key audit partner as being responsible for the audit of material subsidiaries in a group audit and the Audit Technical Advisory Group would be meeting in October to discuss the guidance on this matter.

**10 TAG Update**

- 10.1 The Council noted the Minutes of the TAG meeting held in July and the Rolling Record of Actions which will be updated on the FRC website.

*Staff Guidance Note 05/2016 (Revised) – Prohibited Tax Services*

- 10.2 MB highlighted that the Guidance Note has been reviewed to provide more guidance to practitioners on examples of those services that are considered likely to be subject to prohibition. The Council considered the content of the Guidance Note and was supportive of its publication.

*Staff Guidance Note 02/2017 – Explaining to what extent the audit was considered capable of detecting irregularities, including fraud*

- 10.3 MB provided a brief background on the requirement in the auditor's report to explain to what extent the audit was considered capable of detecting irregularities, including fraud, and that this explanation should be clear and concise, without the use of boiler plate text.
- 10.4 The Council debated the factors that would need to be considered to meet the requirement at length and expressed concern that this could be seen as an extremely broad and onerous obligation on auditors. MB informed that this was the requirement from the Audit Regulation which was brought into ISA (UK) 700 paragraph 45R-1(c) through the copy out procedure and that the proposed guidance was to help auditors to demonstrate how they have met the requirements set out in the law.
- 10.5 In response to a query, MB informed that the matter had been discussed with a couple of EU Member States. The Council queried how important and urgent it was to issue the guidance; it was reported that without guidance there is a risk of inconsistent practice in the UK audit market, and the possibility of UK auditors issuing audit reports that failed to comply with the law. Therefore it was time critical to issue the guidance to address this regulatory gap in the public interest.
- 10.6 Considering the reasons provided, the Council agreed to support the issue of the proposed Guidance Note, and to continue to monitor what happens in practice.

*Working Draft Staff Guidance Note 03/2017 – Providing restructuring services to audited public interest entities through bank lending or bond funded syndicates*

- 10.7 MB informed the Council that the proposed draft Guidance Note had been developed with the help of the TAG Members and an expert working group set up by the TAG. The draft Note had been circulated widely and helpful comments had been received from audit firms. However, an interpretation on one of the aspects of the guidance is subject to advice that the FRC is waiting to receive. It was reported that if the advice requires changes to the draft Guidance Note, the revised version will be circulated to Council. Subject to that, the Council supported the issue of the Guidance Note.

**11 Any other business**

- 11.1 There was none reported.

**12 Date of next meeting**

12.1 The next Council meeting will be on 31 October 2017 at 1pm.