



April 2014

Bulletin 4: Recent Developments in Company Law, The Listing Rules and Auditing Standards that affect United Kingdom Auditor's Reports

The FRC is responsible for promoting high quality corporate governance and reporting to foster investment. We set the UK Corporate Governance and Stewardship Codes as well as UK standards for accounting, auditing and actuarial work. We represent UK interests in international standard-setting. We also monitor and take action to promote the quality of corporate reporting and auditing. We operate independent disciplinary arrangements for accountants and actuaries; and oversee the regulatory activities of the accountancy and actuarial professional bodies.

The FRC does not accept any liability to any party for any loss, damage or costs howsoever arising, whether directly or indirectly, whether in contract, tort or otherwise from any action or decision taken (or not taken) as a result of any person relying on or otherwise using this document or arising from any omission from it.

© The Financial Reporting Council Limited 2014
The Financial Reporting Council Limited is a company limited by guarantee.
Registered in England number 2486368. Registered Office: 5th Floor,
Aldwych House, 71-91 Aldwych, London WC2B 4HN

CONTENTS

Paragraphs

Introduction	1 – 3
The Strategic Report	4 – 16
The Stand-alone “Strategic Report with Supplementary Material”	17 – 29
Auditing the Directors’ Remuneration Report	30 – 49
Changes in Listing Rule requirements with respect to directors’ remuneration disclosures	50 – 53
Recent changes to ISA (UK and Ireland) 700	54 – 63
Appendices	
1. Example 1 – Non-publicly traded company preparing financial statements under the FRSSE	
2. Example 9 – Publicly traded premium listed group – Auditor’s report on group financial statements prepared under IFRSs as adopted by the European Union	

INTRODUCTION

1. There have been a number of recent developments in UK Company Law, the UK Listing Rules and ISAs (UK and Ireland) that affect both the auditor's duties and the wording of auditor's reports on the financial statements of companies.
2. These developments are:
 - (a) The introduction of the Strategic Report;
 - (b) The option for companies to provide its members with a stand-alone "Strategic Report with Supplementary Material" in place of the company's full accounts and reports. "The Strategic Report with Supplementary Material" replaces the previous option of providing a Summary Financial Statement;
 - (c) Amendment of the Regulations that specify the information to be included in a quoted company's Directors' Remuneration Report;
 - (d) Changes in the requirements of the Listing Rules with respect to directors' remuneration disclosures; and
 - (e) Changes to ISA (UK and Ireland) 700 "The Independent Auditor's Report on Financial Statements" made in October 2012 and June 2013 and the issuance, in November 2013, of a Clarification Statement in respect thereof.
3. The effects of these developments on the auditor's report are illustrated in:
 - Appendix 1: Example 1 from Bulletin 2010/2 (Revised March 2012). Non-publicly traded company preparing financial statements under the FRSSE.
 - Appendix 2: Example 9 from Bulletin 2010/2 (Revised March 2012). Publicly traded premium listed group – Auditor's report on group financial statements prepared under IFRSs as adopted by the European Union.

New text to be inserted is shown as underlined and text to be removed is shown as struck-out.

THE STRATEGIC REPORT

Background

4. The Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013¹ (SI 2013/1970) has amended the Companies Act 2006 (CA 2006) to insert new sections providing for the preparation, by certain companies, of a Strategic Report. The purpose of the Strategic Report is to inform members of the company and help them assess how the

¹ The Regulations are set out in Statutory Instrument 2013 No. 1970.

directors have performed their duty under section 172 (duty to promote the success of the company) of CA 2006.

Duty to prepare strategic report

5. The directors of all companies, other than those entitled to the small companies' exemption, must prepare a strategic report for each financial year of the company. A company is entitled to the small companies' exemption in relation to the strategic report for a financial year if:
 - (a) It is entitled to prepare accounts for the year in accordance with the small companies' regime, or
 - (b) It would be so entitled but for being or having been a member of an ineligible group.
6. If the company is a parent company and the directors prepare group accounts the strategic report must be a consolidated report (a "group strategic report") relating to the undertakings included in the consolidation. A group strategic report may, where appropriate, give greater emphasis to the matters that are significant to the undertaking included in the consolidation, taken as a whole.

Content of strategic report

7. Sections 414C (2) and (3) of CA 2006 require the strategic report to contain:
 - (a) A fair review of the company's business, and
 - (b) A description of the principal risks and uncertainties facing the company.

The review required is a balanced and comprehensive analysis of:

- (a) The development and performance of the company's business during the financial year, and
- (b) The position of the company's business at the end of that year.

The detailed requirements regarding the content of the strategic report are set out in Sections 414C (4) to (14) of CA 2006.

Approval and signing of strategic report

8. The strategic report is required to be approved by the board of directors and signed on behalf of the board by a director or the secretary of the company.

Effective date

9. The Regulations set out in SI 2013/1970 are effective for financial years ending on or after 30 September 2013.

Consequential changes to the content of the Directors' Report

10. There are a number of consequential changes to the content of the Directors' Report. The principal changes are as follows:
- (a) It is no longer a requirement for a Business Review to be prepared as part of the Directors' Report.
 - (b) The Directors' Report no longer requires a statement by the company of its principal activities in the course of the year.
 - (c) A number of detailed changes have been made to the requirements regarding the content of the Directors' Report set out in the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (SI 2008/410) and the Small Companies and Groups (Accounts and Directors' Report) Regulations 2008 (SI 2008/409).

What the auditor needs to do

11. Section 496 of CA 2006 requires the auditor to state in his report on the company's annual accounts whether the information given in the strategic report (if any) for the financial year for which the accounts are prepared is consistent with those accounts. This is the same statutory reporting responsibility as that which applies to the Directors' Report.
12. ISA (UK and Ireland) 720, Section B – "The Auditor's Statutory Reporting Responsibility In Relation To Directors' Reports", deals with the auditor's statutory reporting responsibility in relation to the directors' report. When reporting on the strategic report the auditor applies the requirements and application and other explanatory material in ISA (UK and Ireland) 720, Section B to the extent that they are applicable to the Strategic Report.
13. Under subsection (5)(b) of section 498 of CA 2006 if the directors of a company have taken advantage of the small companies exemption from the requirement to prepare a strategic report and in the auditor's opinion they were not entitled to do so, the auditor is required to state that fact in the auditor's report.

Implications for the illustrative auditor's reports in Bulletin 2010/2 (Revised March 2012)

14. Where the directors of a company prepare a strategic report the bullet point relating to the Directors' Report in the section headed "Opinion on other matters prescribed by the Companies Act 2006" should now read (new text shown as underlined):

- The information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

15. This change applies to examples 2 to 11 in Bulletin 2010/2 (Revised March 2012).
16. Where the directors of a company have taken advantage of the small companies' exemption from the requirement to prepare a strategic report and in the auditor's opinion they were entitled to do so the final bullet point of example 1 in Bulletin 2010/2 (Revised March 2012) is amended as follows:

“We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- ...
- the directors were not entitled to [prepare the financial statements in accordance with the small companies regime] [and] [take advantage of the small companies' exemption in preparing the directors' report] [and] [take advantage of the small companies exemption from the requirement to prepare a strategic report]”.

THE STAND-ALONE “STRATEGIC REPORT WITH SUPPLEMENTARY MATERIAL”

Background

17. The Companies (Receipt of Accounts and Reports) Regulations 2013² (SI 2013/1973) establish the circumstances under which a company may send to its members, in place of the company's full accounts and reports, a copy of the company's “Strategic Report with supplementary material” in accordance with section 426 of CA 2006.
18. Section 426 of CA 2006 (as originally enacted) provided that a company could send a summary financial statement to persons who were entitled to receive full copies of the company's accounts and reports. That section was amended by SI 2013/1970 to substitute for a “summary financial statement” a copy of the “strategic report and supplementary material”.
19. The requirement for a company to prepare a strategic report is set out in section 414A of CA 2006 and what constitutes “supplementary material” is described in section 426A of CA 2006 as inserted into the Act by SI 2013/1970.
20. The supplementary material is required to:
- (a) Contain a statement that the strategic report is only part of the company's annual accounts and reports;

2 The Regulations are set out in Statutory Instrument 2013 No. 1973.

- (b) State how a person entitled to them can obtain a full copy of the company's annual accounts and reports;
 - (c) State whether the auditor's report on the annual accounts was unqualified or qualified and, if it was qualified, set out the report in full together with any further material needed to understand the qualification;
 - (d) State whether, in that report, the auditor's statement under section 496 (whether strategic report and directors' report consistent with the accounts) was unqualified or qualified and, if it was qualified, set out the qualified statement in full together with any further material needed to understand the qualification; and
 - (e) In the case of a quoted company, contain a copy of that part of the directors' remuneration report which sets out the single total figure table in respect of the company's directors' remuneration in accordance with Schedule 8 to the Large and Medium-sized Companies (Accounts and Reports) Regulations 2008 (SI 2008/410).
21. The expression "qualified" in (c) and (d) above has the following meaning as set out in section 539 of CA 2006:

"'qualified', in relation to an auditor's report (or a statement contained in an auditor's report) means that the report or statement does not state the auditor's unqualified opinion that the accounts have been properly prepared in accordance with this Act or, in the case of an undertaking not required to prepare accounts in accordance with this Act, under any corresponding legislation under which it is required to prepare accounts."

22. Regulation 2 of SI 2013/1973 revoked the Companies (Summary Financial Statement) Regulations 2008 (SI 2008/374). Regulations 4 to 8 provide for the conditions under which a company may provide a copy of the strategic report with supplementary material and the procedures by which it can be ascertained whether a person wishes to receive full accounts and reports. These regulations are in substantially the same form as regulations 4 to 8 of SI 2008/374.

Effective date

23. The Regulations set out in SI 2013/1973 are effective for financial years ending on or after 30 September 2013.

What the auditor needs to do

Repeal of requirement for an auditor's statement

24. Sections 427(4)(d) and 428(4)(d) of CA 2006 as originally enacted required summary financial statements to contain a statement by the company's auditor of its opinion as to whether the summary financial statement is consistent with the full annual financial

statements and the Directors' Report and complies with the applicable requirements of the Companies Act 2006 and the regulations made thereunder.

25. These requirements have been repealed and the newly inserted requirements relating to a stand-alone "Strategic Report and Supplementary Material" (i.e. one that is not included in the Annual Report) do not require a statement by the company's auditor to be included.

The auditor's procedures

26. When planning the audit of a company the auditor ascertains whether a stand-alone "Strategic Report and Supplementary Material" will be prepared for distribution to those members who elect to receive it instead of the full annual reports and accounts. If so, the audit engagement letter, or a separate engagement letter, records the respective responsibilities of the directors and the auditor with respect to the stand-alone Strategic Report.
27. In order for the auditor to carry out its work on the stand-alone "Strategic Report and Supplementary Material" at the same time as it completes the audit, the auditor encourages the directors to plan the year end timetable accordingly.
28. The auditor's procedures in relation to the stand-alone "Strategic Report and Supplementary Material" are:
 - (a) Ensuring that the stand-alone strategic report is the same as the strategic report published in the annual report and accounts. Once the auditor has established that the stand-alone strategic report is the same as that included in the annual report no further work is required if the procedures outlined in paragraphs 11 to 13 have been satisfactorily completed; and
 - (b) Assessing whether the requirements of CA 2006 with respect to the Supplementary Material have been complied with.

Implications for the illustrative auditor's reports in Bulletin 2010/2 (Revised March 2012)

29. There are no implications for the illustrative auditor's reports in Bulletin 2010/2 (Revised March 2012).

AUDITING THE DIRECTORS' REMUNERATION REPORT

Background

The responsibility of directors

30. Section 420 of CA 2006 sets out the duty of directors of quoted companies (as defined below) to prepare a directors' remuneration report for each financial year of a company. Section 421 of CA 2006 addresses the content of the directors' remuneration report and provides that the Secretary of State may make provision by regulations as to:

- (a) The information that must be contained in a directors' remuneration report,
- (b) How information is to be set out in the report, and
- (c) What is to be the auditable part of the report.

31. Section 421 of CA 2006 further provides that it is the duty of:

- (a) Any director of a company, and
- (b) Any person who is or has at any time in the preceding five years been a director of the company

to give notice to the company of such matters relating to himself as may be necessary for the purposes of regulations under this section.

32. Section 422 of CA 2006 requires the directors' remuneration report to be approved by the board of directors and signed on behalf of the board by a director or the secretary of the company.

Definition of quoted company

33. For this purpose a quoted company is defined in section 385 of CA 2006 as follows:

- (a) ...a company is a quoted company in relation to a financial year if it is a quoted company immediately before the end of the accounting reference period by reference to which that financial year was determined.
- (b) A "quoted company" means a company whose equity share capital:
 - a. has been included in the official list³ in accordance with the provisions of Part 6 of the Financial Services and Markets Act 2000 (c 8), or
 - b. is officially listed in an EEA State, or
 - c. is admitted to dealing on either the New York Stock Exchange or the exchange known as Nasdaq.

2013 Regulations

34. Effective for year ends ending on or after 30 September 2013 "The Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013"⁴ (SI 2013/1981) came into force. These Regulations amend Schedule 8 "Quoted Companies: Directors' Remuneration Report" of "The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008". Schedule 8 specifies the information to be included in the Directors' Remuneration Report.

3 The "official list" has the meaning given by section 103(1) of the Financial Services and Markets Act 2000.

4 Statutory Instrument 2013 No. 1981.

35. A significant change to Part 3 of Schedule 8 is that it now requires the Directors' Remuneration Report to include a single total figure table of remuneration in respect of each person who was a director during the relevant financial year.

What the auditor needs to do

The auditor's responsibility and duties

36. Section 497 of CA 2006 requires in respect of quoted companies that the auditor in its report on the company's annual accounts for the financial year, must:
- (a) Report to the company's members on the auditable part of the directors' remuneration report, and
 - (b) State whether in its opinion that part of the directors' remuneration report has been properly prepared in accordance with this Act.
37. Section 498 (2) of CA 2006 also requires the auditor of a quoted company to form an opinion as to whether the auditable part of the company's directors' remuneration report is in agreement with the accounting records and returns. If the auditor is of the opinion that the auditable part of the report is not in agreement with the accounting records and returns he is required to state that fact in his report.
38. Section 498 (4) of CA 2006 further requires that if the requirements of regulations under section 421 CA 2006 as to information forming the auditable part of the directors' remuneration report are not complied with in that report the auditor is required to include in the auditor's report, so far as he is reasonably able to do so, a statement giving the required particulars.
39. Section 498 (4) has an identical requirement with respect to the disclosures made under section 412 of CA 2006 (disclosure of directors' benefits: remuneration, pensions and compensation for loss of office in the notes to the accounts). These latter requirements are separate from the requirements relating to the directors' remuneration report (see below).

Provisions of the Directors' Remuneration Report which are subject to audit

40. The information contained in the directors' remuneration report which is subject to audit is the information required by paragraphs 4 to 17 (inclusive) of Part 3 of Schedule 8. This information includes the single total figure table of remuneration described above.

Reporting on the Directors' Remuneration Report

41. As the auditor is not required to audit all of the information contained in the Directors' Remuneration Report the auditor will need, in its report, to describe accurately which elements of the Directors' Remuneration Report it has audited. The auditor, therefore, makes arrangements with the directors, well in advance of the year end, to ensure that

the audited disclosures will be clearly distinguished from those that have not been audited.

42. It would be unsatisfactory for an auditor, in its report, to describe what it has audited in an uninformative manner such as “the disclosures required by Part 3 of Schedule 8 to The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations” as this would require readers of the auditor’s report to have a detailed knowledge of the requirements.
43. The auditor assesses whether the scope of its audit will be capable of being clearly described. If this cannot be achieved to its satisfaction by cross-reference, it sets out the particulars that have been audited within the auditor’s report.

Difference between the disclosures required by Schedule 5 and Schedule 8 of The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008

44. Schedule 5 of the Regulations requires a company to provide certain information concerning directors’ remuneration by way of the notes to the company’s financial statements. The majority of the provisions of Schedule 5 apply only to unquoted companies (as the information required to be disclosed would be duplicated by disclosures in the Directors’ Remuneration Report). However, the provisions described as “Total amount of directors’ remuneration etc.” apply to both quoted and unquoted companies.
45. A consequence of this may be that the financial statements of a quoted company disclose aggregate directors’ remuneration that may differ from the aggregate directors’ remuneration disclosed in the Directors’ Remuneration Report. This may arise because the definition of aggregate remuneration differs between the two Schedules.
46. Both of these disclosures are reported on by the auditor. Where both disclosures have been prepared in accordance with the requirements of the Act and the various Regulations any difference between the disclosures is, prima facie, an inconsistency. However, the difference is not an inconsistency as defined by ISA (UK and Ireland) 720 (Revised October 2012) Section A – “The Auditor’s Responsibilities Relating to Other Information in Documents Containing Audited Financial Statements”. This is because the inconsistency arises from complying with the law and it would, therefore, be inappropriate to “correct” the inconsistency. However, as users may think the inconsistency is a mistake the auditor encourages the directors to provide an explanation of any difference within the Annual Report.

Issuing the Directors’ Remuneration Report as a separate document

47. If a quoted company issues its Directors’ Remuneration Report as a separate document the scope of the auditor’s report included in the Annual Report will, nevertheless, encompass the auditable part of the Directors’ Remuneration Report. For this reason the requirements of ISA (UK and Ireland) 720 (Revised October 2012) Section A apply to the

content of a separate Directors' Remuneration Report, notwithstanding the fact that the Report is not included in a document containing audited financial statements.

48. When the Directors' Remuneration Report is issued as a separate document, although not required by the Act, the auditor:
- (a) When its report is unqualified, encourages the directors to indicate within the Directors' Remuneration Report where the auditor's report, prepared in accordance with section 495 of CA 2006, may be found; or
 - (b) When its report expresses either a qualified or adverse opinion or disclaims an opinion, which is relevant to the Directors' Remuneration Report, require the directors to reproduce the relevant parts of the auditor's report as part of the Directors' Remuneration Report. In the event that the directors do not agree to do so, the auditor considers whether to resign.

Implications for the illustrative auditor's reports in Bulletin 2010/2 (Revised March 2012)

49. These changes have no implications for the illustrative auditor's reports in Bulletin 2010/2 (Revised March 2012).

CHANGES IN LISTING RULE REQUIREMENTS WITH RESPECT TO DIRECTORS' REMUNERATION DISCLOSURES

Background

50. On 12 December 2013 the Financial Conduct Authority (FCA) amended the Listing Rules to delete Listing Rules 9.8.11R and 9.8.12R. These Listing Rules had required premium listed companies to ensure that their auditors review certain disclosures of directors' remuneration and to provide in the auditor's report details of any non-compliance.
51. These Listing Rules were deleted in response to the new Directors Remuneration Reporting Regulations (SI 2013/1981) and Strategic Report Regulations (SI 2013/1970), outlined above, with the intention of reducing unnecessary administrative burdens for a premium listed company incorporated in the UK. The FCA commented "We consider that only having to comply with one set of requirements in relation to most remuneration related disclosures should ensure a simpler and more effective regime for firms".

Effective date

52. The changes apply to premium listed companies with a financial year ending on or after 30 September 2013 that had not published their annual financial report on or before 13 December 2013.

Implications for the illustrative auditor's reports in Bulletin 2010/2 (Revised March 2012)

53. In illustrative examples 4, 8 and 9 the following amendments should be made in the section headed "Under the Listing Rules we are required to review:"

Under the Listing Rules we are required to review:

- the directors statement [set out [on page...]], in relation to going concern; and
- the part of the Corporate Governance Statement relating to the company's compliance with the nine provisions of the ~~{June 2008 Combined Code}~~ [UK Corporate Governance Code^{26 37 42}]-specified for our review; ~~and~~
- ~~certain elements of the report to the shareholders by the Board on directors' remuneration~~^{26 38 40}.

RECENT CHANGES TO ISA (UK AND IRELAND) 700

Background

Changes applicable to all auditor's reports

54. Following changes made to ISA (UK and Ireland) 720A "The Auditor's Responsibilities Relating to Other Information in Documents Containing Audited Financial Statements" a consequential change was made to the required description of the scope of an audit prescribed by paragraph 16 (c) of ISA (UK and Ireland) 700. The change required the following wording to be added to the penultimate sentence of the description.

In addition, we read all the financial and non-financial information in the *[describe the annual report]* to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit.

This change is required to be made to all of the example auditor's reports set out in Bulletin 2010/2 (Revised March 2012).

Changes applicable in respect only of entities that apply the UK Corporate Governance Code

55. Other recent changes to ISA (UK and Ireland) 700 apply only to entities that apply the UK Corporate Governance Code. The following paragraphs provide an overview of these developments.
56. In September 2012 the FRC revised a number of ISAs (UK and Ireland) in order to give effect to the proposals in *Effective Company Stewardship: Next Steps* published by the

FRC in September 2011, and to support changes to the UK Corporate Governance Code and Guidance for Audit Committees that were also issued in September 2012.

57. The changes in the ISAs (UK and Ireland) were mainly directed at:
- (a) Enhancing auditor communications by requiring the auditor to communicate to the audit committee information that the auditor believes the audit committee will need to understand the significant professional judgments made in the audit; and
 - (b) Extending auditor reporting by requiring the auditor to report, by exception, if the board's statement that the annual report is fair, balanced and understandable is inconsistent with the knowledge acquired by the auditor in the course of performing the audit, or if the matters disclosed in the report from the audit committee do not appropriately address matters communicated by the auditor to the committee.
58. In order to reflect these changes in the auditor's report the following text is included under the heading "Matters on which we are required to report by exception".

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

Under the ISAs (UK and Ireland), we are required to report to you if, in our opinion, information in the annual report is:

- materially inconsistent with the information in the audited financial statements; or
- apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Group acquired in the course of performing our audit; or
- is otherwise misleading.

In particular, we are required to consider whether we have identified any inconsistencies between our knowledge acquired during the audit and the directors' statement that they consider the annual report is fair, balanced and understandable and whether the annual report appropriately discloses those matters that we communicated to the audit committee which we consider should have been disclosed.

59. In June 2013 the FRC, following consultation, made further changes to ISA (UK and Ireland) 700 requiring auditors reporting on entities which apply the UK Corporate Governance Code to explain more about their work. In overview the auditor's report is required to:
- (a) Describe those assessed risks of material misstatement identified by the auditor that had the greatest effect on:

- a. The overall audit strategy;
 - b. The allocation of resources in the audit;
 - c. Directing the efforts of the engagement team.
- (b) Provide an explanation of how the auditor applied the concept of materiality in planning and performing the audit; and
- (c) Provide an overview of the scope of the audit, showing how this addressed the risk and materiality considerations.
60. This explanation follows the opinion on the financial statements and is reflected in the example auditor's reports as follows:

Our assessment of risks of material misstatement

[Insert a description of those specific assessed risks of material misstatement that were identified by the auditor and which had the greatest effect on the audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team.]

Our application of materiality

[Insert an explanation of how the auditor applied the concept of materiality in planning and performing the audit. Such explanation shall specify the threshold used by the auditor as being materiality for the financial statements as a whole.]

An overview of the scope of our audit

[Insert an overview of the scope of the audit, including an explanation of how the scope addressed the assessed risks of material misstatement and was influenced by the auditor's application of materiality.]

[The disclosures about the above three matters are made in a manner that complements the description of significant issues relating to the financial statements required to be set out in the separate section of the annual report describing the work of the audit committee in discharging its responsibilities (see paragraphs [19B] and A13D) of ISA (UK and Ireland) 700.]

Effective date

61. All of the above changes to ISA (UK and Ireland) 700 are effective for audits of financial statements for periods commencing on or after 1 October 2012. Although expressed differently this is the same effective date as applies to the legal and regulatory requirements described in paragraphs 4 to 53.

Clarification Statement

62. In November 2013 the FRC issued a clarification statement in respect of paragraph 19A of ISA (UK and Ireland) 700. The clarification statement addresses an issue raised by a number of stakeholders who sought clarification as to whether the requirements of paragraph 19A of ISA (UK and Ireland) 700 are intended to apply with respect to the auditor's report of both the group and the parent company financial statements.

63. The text of the clarification statement can be found on the following page of the FRC's web-site.
<https://frc.org.uk/Our-Work/Publications/Audit-and-Assurance-Team/ISA-700-Clarification-Statement.pdf>

Example 1 – Non-publicly traded company preparing financial statements under the FRSSSE

- *Company qualifies as a small company.*
- *Company does not prepare group financial statements.*

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF XYZ LIMITED

We have audited the financial statements of (name of company) for the year ended ... which comprise [specify the titles of the primary statements such as the Profit and Loss Account, the Balance Sheet, [the Cash Flow Statement], the Statement of Total Recognised Gains and Losses, [the Reconciliation of Movements in Shareholders' Funds]] and the related notes⁵. The financial reporting framework that has been applied in their preparation is applicable law and the Financial Reporting Standard for Smaller Entities [(Effective April 2008)]⁶ (United Kingdom Generally Accepted Accounting Practice applicable to Smaller Entities).

Respective responsibilities of directors and auditor

As explained more fully in the Directors' Responsibilities Statement [set out [on page ...]], the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's [(APB's)] Ethical Standards for Auditors[, including "APB Ethical Standard – Provisions Available for Small Entities (Revised)"]⁷, in the circumstances set out in note [x] to the financial statements⁷.

Scope of the audit of the financial statements

Either:

A description of the scope of an audit of financial statements is [provided on the APB's website at www.frc.org.uk/auditscopeukprivate] / [set out [on page ...] of the Annual Report].

-
- 5 Auditor's reports of entities that do not publish their financial statements on a website or publish them using 'PDF' format may refer to the financial statements by reference to page numbers.
 - 6 Specify the version of The Financial Reporting Standard for Smaller Entities.
 - 7 Delete the words in square brackets if the relief and exemptions provided by ES PASE are not utilised. Paragraph 22 of ES PASE requires disclosure in the auditor's report where the audit firm has taken advantage of an exemption provided by ES PASE. The Appendix to ES PASE provides illustrative disclosures of relevant circumstances where the audit firm has taken advantage of an exemption provided by ES PASE.

Or:

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the *[describe the annual report]* to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit⁸. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at and of its profit [loss] for the year then ended⁹;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice applicable to Smaller Entities; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.¹⁶

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or

⁸ See paragraph 54 for explanation of change.

⁹ Guidance for auditors when a company takes advantage of the option in section 444(1) of CA 2006 not to file the profit and loss account or the directors' report is set out in paragraph 12 of APB Bulletin 2008/4 "The Special Auditor's Report on Abbreviated Accounts in the United Kingdom".

Bulletin 4 April 2014

- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit; or
- the directors were not entitled to [prepare the financial statements in accordance with the small companies regime] [and] [take advantage of the small companies' exemption in preparing the directors' report] [and] [take advantage of the small companies exemption from the requirement to prepare a strategic report]¹⁰.

[Signature]

John Smith (Senior statutory auditor)

for and on behalf of ABC LLP, Statutory Auditor

Address

Date

¹⁰ See paragraph 16 for explanation of change.

Example 9 – Publicly traded premium listed group – Auditor’s report on group financial statements prepared under IFRSs as adopted by the European Union

- *Company is a quoted company and has a premium listing.*
- *Corporate governance statement reported on in the auditor’s report on the group financial statements and incorporated into the directors’ report, either directly or by incorporation by reference as explained in APB Bulletin 2009/4 (see example 7 for an illustration of an auditor’s report where the corporate governance statement is not incorporated into the directors’ report).*
- *Directors’ Remuneration Report reported on in the auditor’s report on the parent company financial statements.*
- *Company does prepare group financial statements.*

INDEPENDENT AUDITOR’S REPORT TO THE MEMBERS OF XYZ PLC

We have audited the group financial statements of (name of company) for the year ended ... which comprise [specify the titles of the primary statements such as the Group Statement of Financial Position, the Group Statement of Comprehensive Income, the Group Statement of Cash Flows, the Group Statement of Changes in Equity]¹¹ and the related notes¹². The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

Respective responsibilities of directors and auditor

As explained more fully in the Directors’ Responsibilities Statement [set out [on page ...]], the directors are responsible for the preparation of the group financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the group financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board’s [(APB’s)] Ethical Standards for Auditors.

11 The names used for the primary statements in the auditor’s report should reflect the precise titles used by the company for them.

12 Auditor’s reports of entities that do not publish their financial statements on a website or publish them using ‘PDF’ format may refer to the financial statements by reference to page numbers.

Scope of the audit of the financial statements

Either:

A description of the scope of an audit of financial statements is [provided on the FRC's website at www.frc.org.uk/auditscopeukprivate] / [set out [on page ...] of the Annual Report].

Or:

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the *[describe the annual report]* to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit¹³. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the group financial statements:

- give a true and fair view of the state of the group's affairs as at and of its profit [loss] for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006 and Article 4 of the IAS Regulation.

Our assessment of risks of material misstatement

[Insert a description of those specific assessed risks of material misstatement that were identified by the auditor and which had the greatest effect on the audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team.]

¹³ See paragraph 54 for explanation of change.

Our application of materiality

[Insert an explanation of how the auditor applied the concept of materiality in planning and performing the audit. Such explanation shall specify the threshold used by the auditor as being materiality for the financial statements as a whole.]

An overview of the scope of our audit

[Insert an overview of the scope of the audit, including an explanation of how the scope addressed the assessed risks of material misstatement and was influenced by the auditor's application of materiality.]

[The disclosures about the above three matters are made in a manner that complements the description of significant issues relating to the financial statements required to be set out in the separate section of the annual report describing the work of the audit committee in discharging its responsibilities (see paragraphs [19B] and A13D) of ISA (UK and Ireland) 700]¹⁴.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Strategic Report and the¹⁵ Directors' Report for the financial year for which the group financial statements are prepared is consistent with the group financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

Under the ISAs (UK and Ireland), we are required to report to you if, in our opinion, information in the annual report is:

- materially inconsistent with the information in the audited financial statements; or
- apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Group acquired in the course of performing our audit; or
- is otherwise misleading.

In particular, we are required to consider whether we have identified any inconsistencies between our knowledge acquired during the audit and the directors' statement that they consider the annual report is fair, balanced and understandable and whether the annual report appropriately discloses those matters that we communicated to the audit committee which we consider should have been disclosed¹⁶.

14 See paragraphs 59 to 60 for explanation of change.

15 See paragraph 14 for explanation of change

16 See paragraph 57 to 58 for explanation of change.

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- the directors' statement, [set out [on page...]], in relation to going concern; and
- the part of the Corporate Governance Statement relating to the company's compliance with the nine provisions of the ~~[June 2008 Combined Code]~~ [UK Corporate Governance Code¹⁷] specified for our review; ~~and~~
- ~~certain elements of the report to shareholders by the Board on directors' remuneration^{18, 19}.~~

Other matter

We have reported separately on the parent company financial statements of (name of company) for the year ended ... and on the information in the Directors' Remuneration Report that is described as having been audited. [That report includes an emphasis of matter] [The opinion in that report is (qualified)/(an adverse opinion)/(a disclaimer of opinion)].

[Signature]

John Smith (Senior statutory auditor)

for and on behalf of ABC LLP, Statutory Auditor

Address

Date

17 The UK Corporate Governance Code was issued in May 2010 and applies to financial years beginning on or after 20 June 2010.

18 The report on directors' remuneration should clearly identify those elements that have been audited.

19 See paragraph 53 for explanation of change.



Further copies, £8.00 (post free) can be obtained from:

FRC Publications

Lexis House
30 Farringdon Street
London
EC4A 4HH

Tel: **0845 370 1234**

Email: **customer.services@lexisnexis.co.uk**

Or order online at: **www.frcpublications.com**

ISBN 978-0-7545-5167-6



9 780754 551676