

AUDIT AND ASSURANCE COUNCIL

**Minutes of a meeting of the Audit and Assurance Council of the FRC
held on 13 February 2017 at the FRC, 8th Floor, 125 London Wall, London, EC2Y 5AS**

PRESENT

Ray King	Chairman
Oliver Beroud	Member
Bryan Foss	Member
Jane Fuller	Member
Kari Hale	Member
Sue Harris	Member
Scott Knight	Member
Stephen Oxley	Member

OBSERVERS

Lee Piller (FCA)
Michael Gaull (PRA)
Michael Kavanagh (IAASA)

IN ATTENDANCE

Kate Acott	Project Director
Mark Babington	Deputy Director of Audit Policy
Anu Bhartiya	Committee Secretary
Melanie McLaren	Executive Director of Audit
Lara McSweeney	Governance Associate & Data Co-ordinator
Daniel Rouse	Lawyer
Marian Williams	Director of Audit

Welcome and apologies

The Chairman welcomed everyone to the meeting and in particular Lara McSweeney, Governance Associate & Data Co-ordinator and Daniel Rouse, Enforcement Lawyer who were attending the meeting as observers. Apologies were noted from Paul Cox, Connall O'Halloran and Jerry Wedge.

1 Minutes and Rolling Actions

Minutes

1.1 The minutes of the Audit & Assurance Council meeting held on 16 January 2017 were approved for publication subject to a correction to the attendee list.

Rolling actions

1.2 The matters arising log was noted.

1.3 High Quality Audit – In response to a query as to how the definition of the High Quality Audit would be disseminated, Mark Babington (MB) reported that the purpose of the definition was to clearly set out what the FRC saw as the components of high quality audit. A concise definition is now available and would be rolled out with the audit committee chairs quality survey for reference, as well as being used in the Developments in Audit Report 2017.

2 Chairman's update

Since the Chairman had not attended the last Board meeting, Melanie McLaren (MM) provided an update on the matters considered by the Board at its meeting on 2 February 2017. The Council noted that the Board had discussed:

- The Government’s green Paper on Corporate Governance Reform with consultation on director’s remuneration, the governance of large private companies and how best to include wider stakeholder view in company decision-making.
- The FRC’s recommendation to the Government to review the enforcement framework in order to establish an effective mechanism for holding directors and other senior positions to account when they fail in their responsibilities.
- The need for greater reflection on how audit firms’ governance are monitored.

3 Report of the Director of Audit Policy

3.1 In the absence of Marek Grabowski (MG), Director of Audit Policy, MB introduced the paper stating that the report of the Executive Director of Audit had not been made available due to its extensive reference to sensitive matters relating to an ongoing ethical case. The following reports, points and observations were made:

- An internal review had been undertaken by the FRC as the UK Competent Authority for regulation of auditors to ensure that we are delivering all of our obligations as Competent Authority and it was confirmed that all obligations were being met.
- ISA 540 – Audit of Accounting Estimates: MG has continued to be heavily involved in Task Force calls in order to finalise the drafting issues in the requirements and some of the supporting application material. It remains a challenge to finalise the standard for the March Board, at the quality that stakeholders, including the FRC, expect.
- IAASB Small and Medium Sized Practices Conference in Paris on 26-27 January 2017– There has been a consistent concern, raised by those who audit smaller entities, about the proportionality and scalability of the international auditing standards in relation to such audits. MG had raised the concept of a “Direct Audit” – one in which the auditor prepared and presented the financial statements from the accounting records and performed an attestation assurance engagement on the accounting records. This would apply a different “audit approach” that would make it clearly distinguishable from the ISA audit and could have particular value in overcoming the self-review threat ethical issues and better align the audit with the skills and knowledge limitations of smaller less complex entities. There was considerable interest in exploring this idea further and the Council may discuss this as a topic for its Away Day in July 2017.
- A licence has now been agreed with IAASA, whereby IAASA will issue an Ethical Standard and ISAs (Ireland) which are based on the FRC’s Ethical Standard and ISAs (UK). That licence also includes the right to use Irish Practice Notes that were developed in conjunction with Chartered Accountants Ireland. The Council agreed the proposal to withdraw the four extant Irish Practice Notes (PN - 10, 15, 19 and 27) as there is no need for the FRC to maintain them or make them available.
- The FRC will be responding to the three Exposure Drafts of IESBA’s Code of Ethics. The draft responses will be presented to the Council at its meetings in April and May. The Council Members were invited to review the Exposure Drafts at the links provided in MG’s report.

3.2 In response to a query, it was clarified that MG attends the IAASB meetings as an independent public member. He is not there as a representative of this Council or the FRC, but represents the public interest.

4 Consultation: ISA (UK) 250 – Consideration of Laws and regulations in an Audit of Financial Statements

4.1 Kate Acott (KA) introduced a suite of papers on the revised ISA (UK) 250 Exposure Draft and Consultation. The proposed revisions to the ISA are limited and replicate the amendments

the IAASB made to the international standard to align the requirements with the revised IESBA Code.

- 4.2 It was noted that the FRC had commented on the IAASB's exposure draft in 2015 highlighting the need for a more fulsome review on ISA 250 in due course. However, the FRC supported the limited amendments introduced by the IAASB, acknowledging the limited scope of the project designed to respond solely to the changes to the revised IESBA Code.
- 4.3 Future consideration should be given to whether Section B of ISA (UK) 250 (Revised) on the statutory duty of auditors to report direct to certain regulators should be updated to align more closely to the requirements of the other ISAs (UK); however, given the limited amendments being made to ISA (UK) 250 (Revised), only conforming amendments are currently proposed for Section B of ISA (UK) 250 (Revised).
- 4.4 ISA (UK) 250 (Revised) includes some limited guidance on the auditor's responsibilities in respect of laws and regulations about money laundering, terrorist funding and proceeds of crime. This guidance is supplemented by Practice Note 12 (Revised) *Money laundering – Guidance for auditors on UK legislation*. It was noted that there were some merits in incorporating such guidance into an appendix in ISA (UK) 250 (Revised), but focusing solely on the auditor's responsibilities and excluding some of the background material currently included in the existing Practice Note.
- 4.5 In response to a query, it was clarified that ISA (UK) 250 (Revised) focuses on two categories of laws and regulations: a) those laws and regulations that have a direct effect on the determination of material amounts and disclosures in the financial statements; and b) other laws and regulations that may have a material effect on the financial statements such as money laundering, terrorist funding, proceeds of crime.
- 4.6 The Members debated the comparison of ISA (UK) 240 and 250 in respect of the risk assessment approach used. Since the proposed revision to ISA (UK) 250 is to address revisions made to international standards by the IAASB which come into force later this year, there may remain expectation gaps on the part of users. The FRC raised this with the IAASB in its comment letter which recommended that the IAASB carry out a more comprehensive revision of ISA 250. It was noted that from auditors' point of view, it would be key to have a proper audit plan in place including the areas of operations and associated risk factors, before the commencement of any audit.
- 4.7 MB reported that any help from the Investor Members to support the outreach of the consultation in order to generate more interest and responses from relevant stakeholders, would be much appreciated.
- 4.6 The Council Members agreed to advise the Codes and Standards Committee to recommend to the Board that the Exposure Draft and the Consultation document for the revised ISA (UK) 250 be approved for issue.

5 Project updates

PN 11 – The Audit of Charities in the United Kingdom – Progress update

- 5.1 KA provided an update on the major revisions identified by the Working Group in their first meeting, which were primarily around reporting to charity regulators, planning a charity audit, responding to identified risks and going concern.
- 5.2 It was further reported that:
 - The guidance in respect of reporting to the Charity Regulators will be issued soon and hopefully within the timescales of this project.

- It is aimed to present a proposed revised PN 11 to Council for its consideration and the Advice at the April 2017 meeting.
- KA has been involved in enormous outreach to engage with auditors, including smaller practices who are very active in the charity sector, charities themselves and a number of sectoral organisations. She is also working closely with Charity Regulators covering all of the UK jurisdictions to ensure that the FRC properly reflects the legislative and regulatory context where necessary in the Practice Note.
- Particular issues arising from the application of ISA 720 to charities will be reviewed as part of the revision.

PN 12 – Money Laundering – Guidance for Auditors on UK Legislation

5.3 MB provided an update on the considerations and approaches being undertaken in revising the PN 12 including:

- The awaited issue of the draft regulations by the Treasury on the Fourth Anti-Money Laundering Directive;
- The proposal to withdraw PN 12 and include the material as an appendix to ISA (UK) 250 when the revisions are exposed. The guidance for auditors on Money Laundering would form as a part of the Standard rather than a standalone Practice Note. The Council Members were in principle in support of this proposal.

Project Approval – Standards for Investment Reporting (SIRs) Update

5.4 MB provided an update on the SIRs which are now quite dated and need to be revised in a number of areas. He reported that consideration is to be given whether new material is required to be developed to deal with the audit of qualified financial benefit statements. This would be a challenging and sensitive project as the SIRs are widely used in jurisdictions other than the UK. It will be ensured that an appropriate mechanism is designed through which the relevant stakeholders can engage, including a public consultation.

5.6 In response to a query, it was stated that a Project Director from the Audit Policy Team will work closely with Financial Conduct Authority and the Takeover Panel. In terms of timescale, it is envisioned to undertake the majority of the work this year with a view to finalise in early 2018.

6 Review of the International Standard Setting boards

MB reported that so far 3 meetings of the Working Group have been held to develop proposals to look at the governance and oversight arrangements of the International Standard Setting Boards.

7 Audit Committee Chairs Quality Survey - proposals

7.1 MB introduced the paper giving reference to the audit quality survey of audit committee chairs carried out by the FRC in 2016. Now, the FRC has its own data collected in support of its role as the Competent Authority for Audit, it can contact audit committee chairs directly. FRC proposes to run the survey directly this year, using the YouGov to provide technology platform to send out the survey. The Council discussed the proposals to amend the survey in 2017, and provided advice in respect of how the survey could be taken forward for this year. The discussion included the following points and observations:

- There was value in receiving comments and feedback from the audit committee chairs rather than receiving scores to questions.
- In 2016, 12 questions were asked to about 370 – 380 respondents and 192 responses were received. It was suggested that, an introductory letter from the Chief Executive or the Executive Director of Audit highlighting the importance of the survey might help to maximise the response rate.

- A review of the questions should be made in order to eliminate overly long or overlapping issues.
 - Questions could include horizon scanning into any emerging issues that the audit committee chairs are concerned about.
 - The audit tendering question could relate to the engagement process and outcome of having an audit quality dialogue between auditor and the audit committee rather than the overall process of tendering.
 - FRC needs to ensure that there is an appropriate representation from unlisted insurers.
- 7.2 Ongoing, it was clarified that there was no attempt to reconcile the scores with AQR as the AQR reflects only a sample of audit and not the overall service level of audit. The FRC reviews the outputs and outcomes as well as the process from all perspectives.
- 7.3 In response to a query, it was reported that the draft survey questionnaire will be presented to the Council before it is issued for response from mid-April through to mid-May to allow audit committee chairs to report any findings in development in audit report.

8 Any other business

Enforcement update

- 8.1 At the request of the Chairman, Daniel Rouse gave an update on the overall process in managing the disciplinary matters for accountants, accountancy firms and actuaries in the UK.

Council Effectiveness review

- 8.2 The Chairman introduced the paper highlighting the overall positive comments received from the members in respect of the Council Effectiveness survey. In addition to the actions as listed in the paper, through discussion, the following points, actions and observations were made:
- The Council to have more input on building the 'Meeting Agendas' by discussing the forward agenda at every meeting.
 - Briefings on IAASB topics should identify the key policy items which are important to the FRC to provide a good basis for understanding MG's input to IAASB discussions.
 - Council to receive a presentation from FRC staff on risk and horizon scanning and understand how risks are reported to the FRC Board
 - It would be helpful to understand the views of the Codes and Standards Committee on Council's overall performance and issues to focus upon.
 - In future Effectiveness Reviews, it would be useful to include views of the Observers and the Management in addition to those of Council members. The summary report should classify where the messages are coming from i.e. Members or Observers or the Management.
- 8.3 A Member of Council informed that his firm has a note to share regarding the interpretation of ISA 720 and whether it should be seen as requiring positive assurance. It was suggested that the note could be shared with this Council and the Audit Technical Advisory Group for discussion.
- 8.4 MM informed that an AQR thematic review will be undertaken on the FRC auditors in respect of their discharging of audit responsibilities.
- 8.5 The next meeting of the Council – 21 March 2017.