



**Minutes of a meeting of the Audit and Assurance Council of the FRC  
held on 30 November 2017 at the FRC, 8<sup>th</sup> Floor, 125 London Wall, London, EC2Y 5AS**

**PRESENT**

Sue Harris	Chair
Mary Cleary	Member
Paul Cox	Member
Bryan Foss	Member
Jane Fuller	Member (from Minute 5.3)
Kari Hale	Member (from Minute 5.3)
Scott Knight	Member
Stephen Oxley	Member
Jerry Wedge	Member

**OBSERVERS**

Michael Gaull (PRA)  
Shelagh McAlpine (IAASA)

**IN ATTENDANCE**

Kate Acott	Project Director
Mark Babington	Deputy Director of Audit Policy
Anu Bhartiya	Committee Secretary
Keith Billing	Project Director
Susan Currie	Head of Delivery & Risk (for Minute 9)
Danielle Davies	Ernst & Young (from Minute 6.1 to 6.3)
James Ferris	Project Director
Andrew Clewer	Ernst & Young (from Minute 6.1 to 6.3)
Marek Grabowski	Director of Audit Policy
Karl Havers	Ernst & Young (from Minute 6.1 to 6.3)
Melanie McLaren	Executive Director, Audit & Actuarial Regulation
Rebecca Smart	Risk & Assurance Manager (for Minute 9)

**1. Welcome and apologies**

1.1 The Chair welcomed everyone to the meeting. Apologies were noted from Council Member Olivier Beroud and Lee Piller (FCA Observer).

*Information Security Policies*

1.2 The Chair enquired if the Council Members had any queries / concerns relating to the revised Information Security Policies, so that Kate Cobill, Assistant General Counsel could be invited to the meeting to answer them. The Members had no queries and the Policies were taken as read.

**2 Declaration of conflict of interest**

There were none reported.

### **3. Minutes and Rolling Actions**

#### *Minutes*

- 3.1. The Council approved the minutes of the Audit & Assurance Council meeting held on 31 October 2017 for publication.

#### *Rolling actions*

- 3.2. The matters arising log which included rolling actions from previous meetings was noted.

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

- 4.1 The Chair provided an update on the matters considered at the Codes & Standards Committee meeting held on 21 November 2017. Among other matters, the Committee had approved for publication the Revised Preliminary Announcements Bulletin, the Money Laundering Feedback Statement and Impact Assessment and the Appendix to ISA (UK) 250, Section A, (Revised December 2017).
- 4.2 The Council noted that the FRC Board will be meeting on 6 December 2017.

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

- 5.1 The Council noted the contents of the Report of the Director of Audit Policy. Following a query in relation to the iXBRL tagging, it was reported that the FRC has raised concerns in response to a consultation with ESMA and the European Commission. The issue is still pending. It is likely that the UK approach in respect of this and other related issues will depend on the outcome of Brexit negotiations.
- 5.2 In response to a query in relation to the continuing resourcing pressures faced by the Audit & Assurance Team, it was reported that the Team continues to carefully prioritise work to deal with the agreed work programme and matters that require urgent attention.

#### *FRC Strategy for 2018-21 Plan and Budget*

- 5.3 The Council considered the FRC Strategy for 2018 – 21 and the proposed work programme. A number of comments and observations were made in respect of audit and assurance matters including that:
- The FRC should have an 'influential role' with national and international bodies to ensure that high quality audit and assurance meets investor and public expectations.
  - Should the FRC invest resources to develop an SMP or SME audit approach as part a longer-term programme?
  - There is an expectation gap between the role of the FRC in raising audit quality through the development of standards and guidance at a national and international level and the perception that the scope of audit does not fulfil the wider needs of society.
  - The FRC should consider how it might expand or build on the work with Independent Non-Executive Members of UK Audit Firms to persuasively set out the purpose and value of audit to address public expectation gaps.
  - The UK audit market in the medium term should be focused on high quality assurance, be increasingly competitive and support stakeholder confidence. This can be supported by the FRC's monitoring, enforcement and thematic reviews.
  - The focus of the work programme for the next three years in relation to audit and assurance is different from that for actuarial and corporate reporting matters. This is due to the focus on the post implementation review of revisions made to ISAs and the FRC Ethical Standard as part of implementation of the EU Audit Regulation and Directive and the FRC's review of ethical matters.
  - The implementation of the new strategy on audit firm supervision will link with the AQR project on culture, leadership and the effectiveness of the firms.

- ‘Raising the bar on audit quality’ could better link rising auditing standards and the AQR inspection and thematic activity against those standards.
- The deliverable ‘setting KPIs with the bodies in relation to Audit Monitoring’ stems from the requirements in the 2016 EU Audit Regulation and Directive wherein professional bodies are required to develop audit quality KPIs as a way of tracking their performance and audit quality.
- The FRC’s strategy of making changes to the Stewardship Code that will establish the foundation for enhanced quality of UK investor stewardship will not be limited to UK investors alone but also world-wide investors in UK listed companies.

## **6 Data and Analytics workshop**

- 6.1 The Chair welcomed Danielle Davies, Andrew Glover and Karl Havers to the meeting. They provided a presentation on ‘Audit of the Future’, which covered the following points:
- The speed of change in technology and individuals adapting to those changes to stay relevant is very quick.
  - The effect on business of changes in technology include job elimination by process automation.
  - Auditing is changing to reflect the speed of technological changes in businesses subject to audit.
  - People engagement surveys in audit show declining job satisfaction. People work longer hours to reach the quality threshold (although there is a question over how reliant they are on following a process).
  - Smaller audit firms use off the shelf technologies and larger firms develop their own technology. There is a need for consistencies and confidence in the integrity of those technologies.
  - There is a need for guidance on how to audit algorithms and other aspects of Artificial Intelligence.
  - Given the pace and quantum of change, it is important not to lose sight of human resources.
- 6.2 The Council discussed that one of the challenges of audit was to make judgements and develop skills to be able to evaluate conclusions. With client technology development and process automation, it is difficult to make professional judgements without understanding how underlying processes work and what assurance they provide. The impact of this is that audit is getting more complex and specialised.
- 6.3 The presenters suggested that although not broken, the ISAs are ambivalent on data analytics, and do not directly encourage their use in an audit of financial statements. They pointed to particular challenges as they saw them including over the use of control testing in a data driven audit. The FRC supports the view that data analytics are compatible with the requirements in the ISAs, and can be a source of assurance subject to being able to gain sufficient appropriate evidence. The Council noted that there is an expectation gap in this area which could be better understood if specific examples and evidence were provided by the presenters to validate their concerns.
- 6.4 The Chair queried whether, if examples were provided, there was any merit in having a discussion on the areas of concern more widely and how these might be addressed. It was reported that the IAASB has established a Data Analytics Working Group to understand the use of data analytics technology and how it is able to enhance audit quality, and this was the forum to discuss potential issues with the standards and to resolve these. It was agreed that if FRC could provide detailed analysis of the challenges, these could be shared with the IAASB Working Group. The FRC would engage with audit firms to facilitate this and the results of this engagement, together with examples will be reported back to the Council.

## **7. IAASB Matters**

### *The Monitoring Group public consultation*

- 7.1 Mark Babington (MB) provided an update on the Monitoring Group's public consultation which will run until 9 February 2018. The consultation sets out options intended to strengthen the governance and oversight of international auditing and ethical standard setting bodies. The consultation paper seeks views on achieving this by making standard setting independent of the auditing/accounting profession. The reforms are also intended to strengthen public interest oversight, by enhancing the role of the Public Interest Oversight Board and developing a framework to ensure that the public interest is served, and to enhance the relevance and timeliness of standard setting. The Monitoring Group also intends to develop a pathway towards a sustainable funding model in the medium-term.
- 7.2 The FRC will respond to the consultation and the Council will be provided with a draft response in early January 2018 for comments, which will then be presented to the Codes & Standards Committee.
- 7.3 In response to a query whether any input has been received from stakeholders, it was reported that the FRC has held engagement meetings with audit firms at global level and undertaken stakeholder outreach. The Monitoring Group will be setting up three global round table meetings of stakeholders and seeking input from investors and corporate communities. Through the membership of The International Forum of Independent Audit Regulators, the FRC has been supporting the work of the Monitoring Group.

## **8 AAT Project Update**

### *Response to IESBA's Consultation – Proposed Revisions to the Code pertaining to the Offering and Accepting of Inducements*

- 8.1 The Council considered the FRC's draft response to the IESBA's Exposure Draft and noted that threats created by inducements with improper intent should be evaluated through the reasonable and informed third party lens. MB confirmed that this proposition was also included by the FRC in a response to an earlier IESBA consultation.
- 8.2 In response to the statement that 'there are no safeguards that can reduce threats created by inducements with improper intent to an acceptable level', a Member viewed that some safeguards in form of corporate culture, policies or sanctions could help reduce risks. However, it was noted that despite the importance of such corporate culture and policies, some inducements could be made with improper intent which are unacceptable and unethical, and that safeguards could not reduce the risk to an acceptable level.
- 8.3 The Council provided its advice in support of the draft response to IESBA, noting that the proposed approach is consistent with the FRC's approach to inducements in the Ethical Standard.

### *Revision of Practice Note 14 – The Audit of Housing Associations in the United Kingdom and Revision of Practice Note 19 – The Audit of Banks and Building Societies in the United Kingdom*

- 8.4 The Council considered the project scoping forms for both Practice Notes 14 and 19. MB reported that there have been significant legal and regulatory changes in the areas of Housing Associations and Banks and therefore, these projects would bring the guidance material up to date with those changes. However, it was noted that the timing of the revision of Practice Note 19 is dependent on the IAASB's work to complete ISA 540.

- 8.5 The Council agreed to provide its advice to the Codes & Standards Committee that it approves the project scoping forms for the revision of Practice Notes 14 and 19.

*Audit firm monitoring and supervision regime update*

- 8.6 The Council noted the proposals for the Audit Firm monitoring and supervision regime document as approved by the FRC Board. Melanie McLaren (MM) reported that the proposals would be covered in the consultation on the FRC's three year Strategy and 2018/19 Plan & Budget. The FRC has outlined the approach to the audit firms in advance of the publication of the consultation.
- 8.7 In response to a query whether the Audit & Assurance Council should be asked to provide its input into this matter, it was noted that the audit firm monitoring and supervision regime do not fall within the remit of the Council, and are the responsibility of the Conduct Committee.

*Staff Guidance Note 03/2017 – The auditor's consideration of materiality relating to other information*

- 8.8 A revised Staff Guidance Note which reflected feedback from TAG Members was tabled at the meeting. Kate Acott (KA) provided a brief background on the purpose of the Guidance Note. The Council noted that the FRC's Accounting & Reporting Policy Team was publishing some frequently asked questions to assist companies with the implementation of the Non-Financial Reporting Regulation within the strategic report. The Guidance Note clarifies the concept of materiality relating to other information reviewed by the auditors and how audit firms should respond to the requirement in accordance with the provisions of ISA (UK) 720 and the legal requirements that apply to Non-Financial Information Statement.
- 8.9 The Council noted that the FRC will be undertaking a thematic review on how firms have addressed the requirements applicable to the audit of other information.
- 8.10 A Member mentioned that the illustrated example on political donations was helpful. However, it was felt that further examples that require careful professional judgement on materiality and the auditor's rationale in making that judgement would be helpful.
- 8.11 Subject to the inclusion of a further example by KA and MB, the Council supported the provision of guidance on the auditor's responsibilities in respect of Non-Financial Reporting and issue of the guidance note.

**9 Risk Management Report**

- 9.1 Susan Currie presented the paper and noted the changes in risks that have taken place since the Council's last discussion on this topic.
- 9.2 In response to a query relating to the programme of deep dives on Principal Risks, it was noted that the programme will begin in the New Year which will involve workshops with relevant staff on each of the Principal Risks. The findings from each deep dive will be discussed with ExCo before being presented to the Audit Committee. The Council will also receive an update on the developments in risk management.
- 9.3 The Council discussed the exposure of reputational risk to the FRC in respect of its supervisory role as competent authority. Following a query, it was noted that the risk around future attractiveness of the audit profession was included in the risk register.

**10 Any other business**

*Council Effectiveness Review*

- 10.1 The Council noted the Council Effectiveness review action log and was content that the actions arising from the Review were completed. MM informed that the Board will be considering proposals for the board effectiveness review for the current year at its next meeting on 6 December 2017.

*Future scoping of audit*

- 10.2 MM informed that the Audit Quality Forum was held on 28 November. It had been agreed with the ICAEW that a coalition be formed to consider how audit in the future can be developed to better meet public interest. The Council was invited to provide ideas for the programme and recommend names of independent persons who might be interested in chairing the coalition.

**11 Date of next meeting**

- 11.1 The next Council meeting will be held on 19 February 2018 at 1pm [This was subsequently changed to 15 March 2018 at 1pm].