

Audit and Assurance Council

Minutes of a meeting of the Audit and Assurance Council of the FRC
held on 16 December 2013 at Aldwych House, 71-91 Aldwych, London WC2B 4HN

PRESENT:

Nick Land (Chair)
Russell Frith
Scott Knight
Robert Talbut (to agenda item 6)
Paul Lee
Allister Wilson

IN ATTENDANCE:

Keith Billing	Project Director
Francesca Chittenden	Council Secretary
Marek Grabowski	Audit Policy Director
Jon Hooper	Project Director
Steven Leonard	Project Director
Mark Mainwaring	Project Director
Melanie McLaren	Executive Director
Gareth Rees	Executive Counsel, Professional Discipline Team

1. Apologies and introduction

- 1.1 Apologies were noted from Sue Harris (Council Member), John Hughes (Council Member), Jon Grant (Director of international Auditing Standards), Ray King (Council Member), Aiden Lambe (CIA observer), Trevor Rushe (IAASA observer) and Pat Sucher (PRA observer).
- 1.2 The Council noted that Jon Grant would shortly be retiring from the FRC and the IAASB and therefore his role on the Council would cease. The Chairman placed on record thanks for the contribution Jon had made to the work of the Council.

2. Minutes of the previous meeting and rolling actions

- 2.1 The minutes of the Audit & Assurance Council meeting of 13 November 2013 were approved as an accurate record of the meeting.
- 2.2 The Council noted that all actions were either complete or addressed on the agenda.

Reports

3. Chairman's Update

3.1 The Chairman provided a verbal summary of the outcome of the Council Effectiveness review that had recently concluded and the actions arising as a result of the review. The Council noted that the findings of the review had been positive and that the actions arising from the review could be considered as continuous improvements.

3.2 Relating to specific actions the Chairman confirmed that:

- efforts to secure an observer from BIS would continue;
- progress was being made in relation to the recruitment of an Irish member;
- the 2014 Council meeting dates would be re-circulated to determine Member availability; and
- the Audit & Assurance Council away day would be rescheduled so that it is held before the FRC Board Strategy day so that the Council have the ability to feed in to the Board's deliberations more fully.

3.3 The Council noted that a repeat of the Council Effectiveness review process would be aligned with the next external review of the FRC Board.

4. Report of the Director of Audit Policy

4.1 Mr Grabowski (MG) introduced his report which was taken as read. Particular emphasis was given to the following matters.

ICAEW response to the IAASB Consultation

4.2 The Council noted that the ICAEW, in its response to the IAASB'S Exposure Draft, had made a number of unwarranted comments about the FRC's commitment to ISAs and auditor reporting and that Melanie McLaren had held a number of discussions with the ICAEW and had written a formal letter to the ICAEW in respect of those comments.

IAASB Meeting held on 9-13 December

4.3 MG provided the Council with feedback of the discussions held at the meeting of the IAASB Board, key points identified and discussed were as follows:

- a) ISA 720 Revised – The auditor's responsibilities relating to other information
 - the Council noted that the IAASB Task Force (of which MG is a member) considers that most aspects of the proposed revised ISA are close to finalisation. However, as some of the terminology proposed in the revised draft has similarity to that included in the proposals of the PCAOB, the Task Force believes it would be appropriate to obtain an understanding of the responses to the PCAOB proposals before requesting that the IAASB vote on a final revised ISA 720;
 - the Council noted that there are still some differences of view in relation to the objectives of the auditor and the work effort;
- the Council noted the revised definition of 'other information' and 'the annual report' and that the scope would not be extended to cover all communications, including preliminary announcements, which were at least as important. In response, MG informed the Council that the IAASB was of the view that preliminary reports should be approached

through a separate project in future. He also noted that, in the UK, the Listing Rules include a requirement that preliminary announcements may not be issued without the agreement of the auditor which is covered by the FRC Bulletin 2008/2 *The Auditor's Association with Preliminary Announcements made in Accordance with the Requirements of the UK and Irish Listing Rules*;

- MG undertook to circulate the note of the meeting once it had been finalised.
- b) Disclosures – the Council noted that the Task Force's proposals relating to Disclosures had been broadly supported but that further consideration was required in relation to ISA 320 and the application of materiality. The Council noted that the changes being proposed mainly comprise additional guidance in the form of application material, rather than adding to or revising requirements, and that the IAASB was expecting to consider proposals draft from the task force for an exposure draft at its March 2014 meeting.
- c) Audit Quality – the Council noted that the IAASB Board had approved the final version of the IAASBs Audit Quality Framework with minimal amendments.
- d) IAASB Future Strategy – the Council noted that the IAASB consultation on its future strategy 2015-19 and related work plan had been approved and would be published shortly.

EU Policy Developments

4.4 The Council noted that final stage triologue negotiations are continuing but that progress had been slowed down due to disagreements over restrictions on non-audit services. However, it was still hoped that reform would be completed by approval of the new Regulation and revised Directive in a plenary vote of the Parliament scheduled for late February.

Improving confidence in the value of audit

4.5 Jon Hooper (JH) introduced a suite of papers which set out an updated project overview, details of the terms of reference (ToR) for the project, proposals for establishing project working groups and a mapping of other initiatives relevant to the project, all of which had been considered by the project steering group the previous week. The Council noted that the FRC had published the draft FRC Plan and Budget 2014/15 and that the project was referred to in the document.

4.6 The Council welcomed the draft project ToR and the key project deliverables. In discussing the possible questions upon which the development of the KPIs might be based the Council highlighted the importance of ensuring that the deliverables could and would be achieved before they are announced publicly and the importance of continuing to monitor market views on the value of audit.

4.7 The Council supported the proposal to establish two project working groups, one to lead on project components 2 & 3 which would be established as the 'Public Interest Group' and one to lead on component 4, which would be established as the 'Audit Quality Group'. The Council discussed the proposed memberships of the working groups and suggested that there should also be representation from companies that are not listed on

the London Stock Exchange. The Council discussed whether or not there was a need for overseas representatives on the groups and concluded that it would be sufficient, and pragmatic, for some International Members to participate on the working groups in an observer capacity. JH invited the Council to forward any recommendations of potential members to the team for consideration.

- 4.8 The Council noted the document which mapped extant audit initiatives and the request from JH to forward any relevant developments or initiatives Members are aware of, or become aware of, to the team for inclusion within the document.

Code of Audit Practice for Local Government Audit

- 4.9 The Council noted the draft revised Code of Audit Practice and the importance of monitoring the development of the Code to ensure the standards set by the FRC is aligned with it.

5. Activities since last meeting

- 5.1 The Council noted the list of activities since the last meeting.

Standards and Guidance

6. PN 14 – Housing Associations

- 6.1 Steve Leonard (SL) introduced the final Practice Note 14 'The Audit of Housing Associations in the United Kingdom'. The Council noted that the FRC had received five responses to the Consultation Paper issued in July 2013 and that all of the respondents had indicated broad and quite strong agreement for the proposals. The Council also noted that although no formal response to the Consultation Paper had been received from the other Regulators they had indicated positive support for the revised PN.

- 6.2 The Council noted that the following minor issues had been identified:

- a) There was a concern that some of the contextual information could be too time specific. In response, with the agreement of the working party, those elements of the text have been left unchanged but the introduction highlights that the PN was written at a specific point in time and that auditors should be actively aware of and alert to the potential changing environment.
- b) It was queried whether the proposed PN makes adequate reference to the risks associated with the issuance of the new SORP and the adoption of FRS 102. FRC staff, and the working party, do not consider it appropriate to provide advice on the application of accounting standards within an auditing PN, however, the PN has been revised to provide greater signposting to the fact the SORP is about to be revised and the reference to FRS 102 has been moved to a more prominent position.
- c) It was commented that the audit of related parties is a challenge to auditors due to the wide ranging backgrounds of non-executive boards and the fact that board members often have links with similar organisations; accordingly material on ISA 550 has been included.
- d) In its response one firm had questioned the accuracy of one element of the guidance in relation to materiality as set out in paragraph 155 of the PN. It was agreed that the guidance was appropriate.

6.3 The Council was content with the approach to the issues identified; accordingly, the Council approved its advice to the Codes & Standards Committee (CSC) to issue PN14. The Council also approved the accompanying advice for the CSC that had been drafted to address the draft criteria the CSC had recently considered for determining when guidance or standards should be issued.

7. Auditor reporting on narrative parts of the Annual Report – ISA (UK and Ireland) 720

7.1 SL introduced a report which set out a proposal that the FRC issue a Bulletin as an interim measure which would set out the issues the revisions to ISA (UK & Ireland) 720 will address in respect of the revisions to ISA 720 the IAASB intend to consider for re-exposure at its meeting in March 2014.

7.2 The Council noted that the Bulletin would address the following specific additions to ISA (UK & Ireland) 720:

- a) the requirements of auditors under CA 2006 with respect to the Director's Remuneration Report;
- b) the requirements of the auditor's statutory reporting responsibility in relation to Directors' Reports to encompass the auditor's responsibilities with respect to the recently introduced Strategic Report; and
- c) The requirements of auditors with respect of corporate governance reports.

7.3 The Council referred again to the draft criteria recently considered by the CSC for determining whether or not there is a need for the FRC to issue guidance or a Standard and discussed whether the Bulletin would meet the criteria set out. Through discussion it was highlighted that:

- it would be helpful to provide auditors with guidance on how the existing standard should be applied in light of the legal changes that have recently come in to force;
- the Bulletin would 'bridge the gap' between the current Standard and the revised standard which will not come in to effect until 2016; and
- the Bulletin would mitigate the risk of inconsistencies in auditor reporting.

7.4 In conclusion the Council agreed to advise the FRC to issue a Bulletin as proposed. The Council suggested that the advice to the FRC should highlight that the same approach to the development of the Bulletin will be followed as was followed in developing the revised PN14.

8. Feedback from the FRC Discipline Team

8.1 The Council received a presentation from Gareth Rees QC (GR), Executive Counsel at the FRC on the work of the FRC Discipline team and the approach of the FRC to investigations and complaints.

8.2 GR drew the Council's attention to the FRC's Accountancy Scheme, a standalone disciplinary Scheme for the accountancy profession maintained by the FRC and in particular, the definition of Misconduct set out in the Scheme.

- 8.3 The Council noted a number of audit cases currently under investigation and the outcome of the recently settled case of Farepak. GR highlighted that although many of the cases considered by the FRC Discipline team are brought against the audit partner, but allegations can also be brought against other individuals involved with the preparation of the audited accounts and the Chair of the Audit Committee.
- 8.4 The Council noted that a number of cases under investigation involve potential Misconduct arising from breaches of APB Ethical Standards and noted it would be much clearer and more accessible if all ethical standards and codes of Ethics were brought together. The Council also discussed issues arising from difficulty in defining public interest but noted that the FRC was building up case law in the area.
- 8.5 The Council noted that particular issues that have arisen in conduct cases which relate to audit include a) reliance on management Representations – professional scepticism, b) the audit of subsidiary entities, c) CASS and d) failures in the responsibilities of Audit Partner and more junior members of the audit team. The Chairman noted that the Council would shortly be asked to consider the development of a Standard for Client Assets and that the needs of the Discipline team would be considered in making that decision.

9. Horizon Scanning discussion

- 9.1 The Chairman introduced the paper and extract of the FRC risk register that relates to the work of the Council, the Council noted that a thorough process had been undertaken to develop the risk register and that it was a comprehensive document.
- 9.2 MM drew the Council's attention to the two relevant programme risks rated as Amber-Red, 'Value of Audit' and 'Enhancing Risk Management Reporting' and highlighted that significant activities were in place to address the risks. It was suggested that the FRC should also look at risks in relation to investor behaviour and the ways to further embed the supporting strategies identified in the register.
- 9.3 The Council noted that the FRC Board will review the Risk Register every six months and that relevant updates would be brought to the Council to inform its deliberations.

10. Any other business

10.1 None.

11. Next Meeting

11.1 The next meeting of the Audit & Assurance Council will be held on Wednesday 22 January 2014 at 9.00am.