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Private & confidential

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Our ref rf

24 September 2019

Dear Mark

Consultation on the proposed revisions to the CASS Standard following post implementation review

We are grateful for the opportunity to provide comment on the FRC's consultation on the Assurance Standard relating to Providing Assurance on Client Assets to the Financial Conduct Authority (respectively referred to as "the Consultation Paper" and "the Assurance Standard"). We welcome the enhancements and additional clarification provided and have considered the proposed changes. Our response provides some specific provisions we would appreciate clarification on.

For ease, we have referred to the annual reporting to the FCA as required by SUP 3.10 of the FCA's Handbook as the "CASS audit". As detailed in the Assurance Standard, the engagement is not an audit and should not be considered as such. However, we have used the generally accepted expression "CASS audit" and "CASS auditor" throughout our response.

Executive Summary

1. We welcome the revised drafting in the provisions to the Assurance Standard that recognises that, in planning and performing the CASS audit, there may be an overlap of procedures between the CASS audit and other statutory audit work and a recognition that the CASS audit will include the use of information technology. We believe this will assist the CASS auditor in scoping and planning the CASS audit.
2. There are some changes which we would be grateful for clarification on, for which we have provided more detailed comments within Appendix I. This includes additions to the Assurance Standard that could potentially impact the reporting responsibilities of the auditor to those charged with governance, the responsibilities of the auditor in ensuring a firm's records are adequate and the reporting on completion of breaches.

3. In our response to the previous consultation submitted on 1 March 2019, we provided some suggested areas that could be enhanced in respect of the limited assurance section. This was in answer to the question on whether there are further steps the FRC should consider including in the CASS Standard to support the delivery of consistently high-quality CASS audits. We would welcome the opportunity to consult the FRC on this, as we believe it would help clarify the requirements of CASS auditors on a limited assurance CASS audit.

We have highlighted specific paragraphs that we would be grateful for further clarification on in Appendix I.

Yours sincerely

Richard Faulkner
Partner, KPMG LLP

Disclosures:

Appendix I: Paragraphs requesting clarification or further consideration of changes

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Amended paragraph in the Assurance Standard	KPMG comment
<p>14 Where the scope of the firm's permissions includes the holding of controlling of client assets and the firm claims that it holds or controls client assets, the CASS auditor shall provide a reasonable assurance Client Assets Report including a breaches schedule as required by the FCA's Rules. In such cases the CASS auditor shall comply with all the requirements of this Standard set out in paragraphs 11 to 1415-and in the case of non-statutory client money trusts also paragraphs 1726 to 17784. However, the FCA's Rules do not require a reasonable assurance Client Assets Report in relation to certain firms in certain circumstances⁴.</p>	<p>We welcome the removal of the requirement to complete a CASS audit on a firm that is only controlling client assets and not holding. We would suggest 'or controls' is also removed from the same sentence in relation to the firm claiming to control client assets (as highlighted in bold) to be internally consistent.</p>
<p>24 The CASS auditor shall accept or continue a Client Asset Engagement only when the CASS auditor:</p> <ul style="list-style-type: none"> a. Has reason to believe that all relevant ethical requirements, including independence, will be satisfied; b. The CASS auditor is satisfied that those who are to perform the engagement, including the CASS engagement leader, have had appropriate training and will have the appropriate competence and capabilities; and 	<p>We recognise the importance of reporting issues to those charged with governance, and understand this to reference the management letter that the CASS auditor will provide to those charged with governance. We would appreciate confirmation that this is the FRC's intention in amending para 24c. A similar clarification is sought on para 135 below.</p>

<p>c. The basis upon which the engagement is to be performed has been agreed between the CASS auditor and the firm, including the CASS auditor's reporting responsibilities to the FCA <u>and to those charged with governance. {See paragraphs 55 to 58 of the Contextual Material).</u></p>	
<p>41 In planning and performing the engagement, the CASS auditor shall also adopt an insolvency mind-set which evaluates the firm's client asset processes on the presumption that the firm may become insolvent <u>{see paragraphs-36—a-RE1-56—ef—the Contextual Material). An insolvency mindset in the context of CASS engagements requires the auditor to ensure that the records maintained by a regulated entity are adequate to identify client assets at any time and without delay to allow their return to the legal owner (CASS 6.6.2 and 7.15.2).</u></p>	<p>We recognise the importance of adopting an insolvency mindset and welcome the FRC taking steps to clarify what that means in the context of a CASS audit. However, the additions as drafted diverge from what an insolvency practitioner would undertake in the event of a firm's insolvency, which is often more complex than simply relying on the firm's records. This would include consideration of whether client assets are adequately segregated from the firm's own assets and money.</p> <p>The additional provisions also require the CASS auditor to "ensure" records are maintained, which conflates the role of the assurance provider with that of management. We suggest amending this wording to require the auditor to "provide assurance" rather than "ensure".</p> <p>Further, the revised drafting intimates that client assets are being held by the firm, and therefore would only be applicable for a reasonable assurance audit. In addition, to make this relevant also for limited assurance CASS engagements where no such records will exist, we recommend the Assurance Standard sets out that the CASS auditor must consider if the firm holds any client <u>assets that may be subject to loss.</u></p>

	diminution or a delay in repatriation in the event of the firm's insolvency.
<p>42 The CASS auditor shall document:</p> <p>a) The overall assurance strategy, <u>including the main areas of engagement risk;</u></p> <p>b) The assurance plan, <u>including the resources that will be deployed to deliver the plan;</u> and</p> <p>c) Any significant changes made during the engagement to either the strategy or the plan and the reasons for making such changes.</p>	<p>We welcome the additional detail provided in para 42. However, we suggest additional wording is included to clarify that engagement risk is intended to refer to the firm's activities, such as products and services offered to clients and business changes, as well as the overarching risks of auditing the entity in accordance with para 15 of the Assurance Standard.</p> <p>Point (b) requires documentation of the resources that will be deployed to deliver the plan. This could be subject to change, and we would suggest the wording is amended to "resources that are planned to be deployed" to allow for any alterations.</p>
<p>86 As the CASS auditor has sole responsibility for the CASS audit opinion, the use of internal auditors to provide direct assistance to a CASS auditor is prohibited in a CASS audit performed in accordance with this Standard. <u>In addition, the CASS auditor's responsibility cannot be reduced by the CASS auditor using the work of the internal audit or</u> <u>se-m-pliance—funstien.</u> However, the CASS auditor is likely to find the work and findings of the internal audit or compliance function to be useful in making its risk assessment. The CASS auditor shall document its conclusion and the basis for this conclusion on how the work and findings of the internal audit or compliance function have impacted on the risk assessment.</p>	<p>We believe your intention in removing the sentence in this paragraph is to be consistent with ISA 315 (UK) on the work of an internal audit or compliance function, and only prohibit direct assistance from internal audit. However the paragraph does not specify in what capacity the CASS auditor can rely on the work of internal audit. We suggest this is enhanced to also confirm what is permitted.</p>

<p>108 The CASS auditor shall plan to perform assurance procedures that cover outsourced functions for which the firm retains responsibility for client assets under the CASS rules. <u>This may include the provision of System and Organisation Control (SOC) Reports. attestina to the adequacy of operating controls in place within the outsourced body. Where the CASS auditor places reliance on such reports, it shall assess the skills, capacity and aualtv of work undertaken by the provider of the SOC Report, and document its assessment and conclusions drawn in the audit file, having taken account of the auditor's own assessment reauired by paragraph 106 of this Standard.</u></p>	<p>We welcome the opportunity to consider placing reliance on SOC Reports. There are however potential complications that we suggest need to be carefully considered when taking this approach. The report may not be sufficiently detailed to form a view on the level of sampling performed or systems covered and hence the reliability the CASS auditor may place on it. Additionally it may not be possible to confirm the independence of the report provider in order to assess whether it aligns with the CASS auditor's independence requirements. On this basis, we believe there are limited circumstances where reliance can be placed on SOC reports in practice due to the challenges noted above.</p>
<p>115 The CASS auditor is required to report all breaches identified by it or identified to it by any other party including the firm. Although a breach may be of minor significance, this is not a relevant consideration when determining if a CASS rule has been breached. The reporting of any breach of a CASS rules shall result in the CASS auditor expressing a modified opinion regarding the adequacy of systems during the period. The reporting of breaches may also result in the need for the CASS auditor to express a modified opinion regarding compliance with the CASS rules at the period-end date. <u>In forming their opinion, the CASS auditor considers the impact of all identified breaches and the effect they would have on the effective operation of the CASS reaime.</u></p>	<p>We would appreciate clarification on what is meant by "the effective operation of the CASS regime". We would suggest this refers specifically to the firm if that is the intention.</p>

<p>135 The CASS auditor shall communicate to management <u>and those charged with governance at an appropriate level of responsibility</u>, on a timely basis, deficiencies in internal control that, in the CASS auditor's professional judgment, are of sufficient importance to merit management's attention. <u>In reporting to management and those charged with governance, the CASS auditor will report those issues which, in the CASS auditor's professional judgment, pose the most significant risk of non-compliance with the CASS rules, and which require the most urgent resolution.</u></p>	<p>We recognise the importance of the auditor using judgment in reporting issues to management that may pose significant risk of non-compliance with the CASS rules, and evidence this through the issuance of a management letter at the conclusion of the audit. We would appreciate confirmation that this is the intended reporting referred to here.</p>
<p>Contextual Material para 37</p> <p>The FCA requires all breaches identified by <u>both</u> the CASS auditor <u>and disclosed to it by the firm</u> to be reported to it <u>by the CASS auditor</u>. <u>The CASS auditor should also provide assurance to the FCA that the CASS firms own reporting of breaches that it has identified are a complete record</u>. The materiality or significance of a breach of the CASS rules, therefore, are not relevant considerations in determining whether the breach of a CASS rule needs to be reported to the FCA by the CASS auditor. For example, a failure to place client money promptly into a segregated client bank account is a reportable breach of the CASS rules regardless of whether the amount concerned is £5 or £5 million.</p>	<p>An amendment has been made to para 37 of the Contextual Material to remove the requirement for the CASS auditor to report breaches disclosed by the firm. This is not supported with changes to the Assurance Standard itself or the Breaches Schedule. It would also suggest a change to the FCA SUP 3 rules would be required in order to be consistent with this approach. We would appreciate clarification on this amendment.</p> <p>The amendment as drafted requires the CASS auditor to provide assurance on the completeness of the firm's breaches register. We do not believe it is possible to provide this assurance without a significant increase in the audit work undertaken by the CASS auditor. We would welcome clarification on whether that is the requirement, and guidance on how that assurance should be obtained.</p>
<p>Deletion of contextual material para 35-9</p>	<p>The contextual material in para 35-9 provides guidance on the requisite mindsets required by a CASS auditor,</p>

*KPMG LLP Consultation on the proposed
revisions to CASS Standard following
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	and disapplication of materiality to a CASS audit. We would suggest this material remains useful when forming the CASS opinion and should remain in the document.
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