



Minutes of a meeting of the Audit & Assurance Council held on Thursday, 14 June 2018 at the FRC Office, 8th Floor, 125 London Wall, London E2Y 5AS

Present:

Sue Harris	Chair of Council
Olivier Beroud	Member
Mary Cleary	Member
Paul Cox	Member (From Minute 1 to 10.5)
Bryan Foss	Member
Jane Fuller	Member
Kari Hale	Member
Scott Knight	Member

Observer:

Michael Gaul	PRA
Lee Piller	FCA

In attendance:

Mark Babington	Deputy Director of Audit Policy
Anu Bhartiya	Committee Secretary
Keith Billing	Project Director
Kate Dalby	Project Director
James Ferris	Project Director
Stephen Haddrill	Chief Executive Officer (From Minute 1 to 3.2)
Josephine Jackson	Technical Director
Erica Nicholson	Project Director (From Minute 1 to 5.7)
Mike Suffield	Director of Audit Quality (For Minute 10)
Marian Williams	Director of Audit (via teleconference) (For Minute 5 only)

Apologies:

Stephen Oxley	Council Member
Jerry Wedge	Council Member
Lisa Campbell	IAASA Observer

1. Welcome and apologies for absence

- 1.1 The Chair welcomed everyone and in particular Mr Haddrill to the meeting. It was noted that Mr Haddrill was present to provide an update on FRC matters in absence of Ms Melanie Hind.

2. Declaration of conflicts of interests

There were none to be reported.

3. Update from the Chief Executive

- 3.1 Mr Haddrill provided an update on the three Board meetings held since the last Council meetings. The discussion at the Board meetings had included:
- the approval of the 2018/21 Strategy document;
 - the FRC's investigation into the audit of Carillion;

- The 'Future of Audit' project which would be led by an independent chair;
 - The consultation on the UK Corporate Governance Code and the Stewardship Code;
 - Wates Principles for the governance of large private companies;
 - The FRC Guidance on Strategic Report;
 - The independent review of the FRC led by Sir John Kingman;
 - The FRC's internal governance review and the approval of terms of references of councils and committees;
 - The FRC Thematic Review on Audit Culture;
 - The Audit Quality Review Public Reports 2018;
 - The Institute of Faculty of Actuaries' draft consultation on the monitoring of actuarial work; and
 - The post-Brexit IFRS endorsement process and the UK audit regime post-Brexit.
- 3.2 In response to a request, it was agreed that the document presenting FRC's strategy on international influence would be circulated to the Council.

4. Minutes of the last meeting and rolling actions

Minutes

- 4.1 The minutes of the Audit & Assurance Council meeting held on 15 March 2018 were approved for publication.

Rolling actions

- 4.2 The matters arising log which included rolling actions from previous meetings was noted. In response to a query in relation to the working group to advise on detailed changes to the SIRs, it was noted that the group would be set up in due course. Mr Beroud offered to join the group as an investor representative.

Council meeting dates for 2019

- 4.3 The meeting dates for the Audit & Assurance Council in 2019 were noted.

5. Audit Firm Information Security and Contingency Planning Review under Audit Firm Monitoring Approach

Information Security Review

- 5.1 Ms Williams provided an update on the scope of the Information Security Review which was on the big six audit firms' risk management and controls over information security arrangements and to form a baseline understanding of the information security policies and procedures. The process included self-assessment of the maturity by the firms in respect of their policies and processes and the FRC's view of their position in relation to others.
- 5.2 The Council noted that the review was conducted on the six largest UK audit firms. Private report based on the self-assessment and FRC's benchmarking and summary of findings has been issued to each firm. The self-assessment included individual firm scores against the overall average scores. Once the FRC is satisfied with the proposed actions to mitigate the key issues identified, the FRC will finalise the reports. Going forward, the FRC will check whether the proposed key actions have been implemented.

Contingency Planning Review

- 5.3 Ms Nicholson provided an update on the scope of the Contingency Planning Review which was to consider the six largest UK audit firms documented approach to contingency planning. The review seeks to identify potential issues with a firm's contingency planning and to invite the firms to propose actions to mitigate the issues identified. This process did not benchmark each firm against the other firms reviewed;

however, the FRC have shared key themes with each of the firms and have received feedback.

- 5.4 In response to a query whether the review was limited to firms' network within the UK only or extended to multi global network, it was clarified that the work was limited within the UK boundaries. However, consideration was given to global network situations as to how the UK firm considered risk from global network and also from a perspective as to how the global network may respond if a UK crisis occurred.
- 5.5 Ms Williams noted that the FRC is a member of the Joint Forum on Audit Firm Contingency Planning and the outcome of the Contingency Planning Review will be shared with the Forum.
- 5.6 The Council noted that the FRC expects to conduct annual reviews of contingency planning going forward. This will include checks whether the proposed key actions have been implemented and seeking more evidence of the contingency plans through firm's use and testing.
- 5.7 A Member suggested that in future AFMA work review could include considering audit firm's business model and financial soundness in light of the economic environment.
- 5.8 Following a query in relation to the plans for finalising the review reports, it was clarified that this falls within the remit of the Conduct Committee. On finalisation, the chair asked the Executive to share the high-level ratings with the Council. The Executive agreed to consider this request. The final report of the review will also be shared with the independent non-executives of the firms.
- 5.9 The Chair thanked Ms Williams and Ms Nicholson for their informative update.

6. Update from the Chair

- 6.1 The Chair noted that the FRC's Governance Event takes place on 27 June and encouraged members to attend. The Chair also noted that the Council Away Day takes place on 13 of September which would start with formal business matters. The draft agenda for the Away Day was tabled at the meeting and the members were invited to send their suggestions if any, on the agenda.
- 6.2 The revised terms of reference of the Council as approved by the Board on 6 June were tabled at the meeting. The Chair highlighted a number of changes that would come into effect from 1 July 2018. The Council noted that its role will be advisory to the FRC Executive on the development and maintenance of high quality, effective and proportionate standards, guidance, SORPS and practice notes for audit and assurance work. This change was aimed to enhance the FRC's agility and speed of process in decision making by requiring only two levels of governance for the approval of material rather than the current three. The Council discussed the scope of its responsibilities on various matters while advising the FRC Executive and noted that:
 - The Terms of Reference have been aligned with those of the Actuarial and the Corporate Reporting Council, where appropriate.
 - Going forward, the Council will provide its advice on standards, which will be approved by the FRC Board. To enhance the speed of process in decision making, the standards will not be routed through the Codes & Standards Committee.
 - The Council will meet 4 times a year as necessary dependent on the annual work plan. Matters of detail will be handled by sub-groups of the Council.
 - Whilst the Council is not responsible for strategy, it shall advise on the FRC Strategy and Annual Plan in so far as it is relevant to the role of the Council.

- Where there is material difference between the view of the Council and the FRC Executive, the Council Chair will report any material concerns to the Board.
- 6.3 The Chair also provided an update on the two meetings of the Codes & Standards Committee held since the last Council meeting. Amongst other matters, the following matters had been discussed:
- The Audit Firm Culture Thematic Review;
 - Actuarial Policy – Transfers from DB to DC Pension Schemes;
 - Accounting and Reporting Policy – Guidance on Strategic Report, Housing SORP, Pensions SORP and Charities SORP;
 - Consultation on the corporate governance principles for large private companies;
 - UK Corporate Governance Code Consultation;
 - An update on Financial Reporting Lab activities.

7. Report of the Director of Audit Policy

- 7.1 Mr Babington introduced his report which provided an update on developments relating to UK and International auditing standards, FRC audit research activities and other FRC matters not covered elsewhere on the agenda. Particular attention was drawn to the following matters:
- The ongoing focus on IAASB projects to which the FRC continues to make major contributions;
 - Stakeholder interest and positive feedback received from the Client Assets Conference in respect of post implementation review project;
 - The ICAEW's decision in respect of the proposed changes to guidance on risk management paragraph (the 'Bannerman paragraph') that the paragraph should be sited at the end of the auditor's report. This had been a positive outcome to achieve.
- 7.2 The Council noted the terms of reference for the independent review of the FRC led by Sir John Kingman.

8. Consultation on UK adoption of ISA 540 (Revised) The Audit of Accounting Estimates and Related Disclosures

- 8.1 Mr Babington outlined the purpose of the paper which was to obtain Council's advice that, once the IAASB approve the ISA 540 (Revised) *Auditing Accounting Estimates and Related Disclosures* together with related conforming amendments to other ISAs at its Board meeting in June 2018, the FRC open a 60-day consultation proposing revision of ISA (UK) 540 and other ISAs (UK) to reflect ISA 540 (Revised) and the conforming amendments to other ISAs. This would enable the effective date to align with the IAASB's.
- 8.2 Through discussion, the Council noted that the FRC's specific concerns and recommendations raised in response to the IAASB ED have been sufficiently addressed in the revised standard and that the FRC does not propose to add supplementary material other than those existing additional requirements and application material included in the current ISA (UK) 540 which bring in relevant requirements from the Audit Regulation and Directive. The Council noted that the feedback received from the 60-day consultation would be presented to Council at its meeting in November 2018.
- 8.3 A Member suggested, following the publication of the revised ISA (UK) 540, it would be helpful to conduct outreach and engagement on the interpretation of the standard, and discuss the requirements in relation to methodologies and documentation. The Executive noted this suggestion and informed that this would be undertaken subject to the availability of resources at the FRC.

- 8.4 The Council advised that once the IAASB approve the ISA 540 (Revised) *Auditing Accounting Estimates and Related Disclosures* together with related conforming amendments to other ISAs, the FRC open a 60-day consultation proposing that the FRC revise ISA (UK) 540 and other ISAs (UK) to reflect ISA 540 (Revised) and the conforming amendments to other ISAs.

9. Analysis of IESBA Restructured Code

- 9.1 Mr Billing provided a brief update outlining that the IESBA has issued its restructured code *International Code of Ethics for Professional Accountants (including International Independence Standards)* which comes into effect in June 2019. Though the FRC does not adopt the IESBA Code, the FRC Ethical Standard (ES) is intended to adhere to the corresponding principles of the IESBA Code. A review of the Restructured Code with the FRC's ES has been conducted and concluded that there are relatively small number of IESBA provisions that are, or could be perceived to be, more stringent than the FRC's ES. The differences are not sufficiently significant to merit revising the Ethical Standard before the completion of the post-implementation review later in 2019 as the current principles-based approach in the ES should drive appropriate ethical outcomes.
- 9.2 The Council gave due consideration to the areas where ES requirements and/or guidance are perceived to be less stringent. The Council made a number of observations in relation to 'breaches' and 'financial interests' as set out in the FRC's ES which were perceived to be less stringent than the IESBA's Restructured Code and concluded that the matters were relatively small which could be addressed when the wider post implementation review of the ES is undertaken.
- 9.3 The Council agreed to support the recommendation that it would be appropriate to wait until the wider post implementation review is undertaken to address specific differences to IESBA's Restructured Code and thereby avoiding the possibility of more than one revision in a relatively short space of time. As part of the post implementation review of the ES, consideration should be given whether requirements and/or guidance should be updated to ensure that the ES is not perceived to be less stringent than the Restructured Code in any significant areas.

10. AAT Project Update

Update on Going Concern project

- 10.1 The Council noted that once the IAASB approves the ISA 315 *Identifying and assessing the risks of material misstatement through understanding the entity and its environment* at its next Board meeting, the mapping of ISA 570 *Going Concern* to ISA 315 will begin. This will include the review of extant guidance in various Bulletins, taking into consideration feedback from the AQR reviews of going concern issues, feedback from Enforcement on completed cases relating to going concern, review of examples of auditor reporting on going concern under new regime (key audit matters, reporting by exception) and joined up working with the Audit Quality Review's ISA 720 thematic review in respect of viability statement.
- 10.2 The Council noted the proposed timetable in respect of the project and queried if December, considering the holiday period, would be the right time to issue consultation. It was clarified that the consultation would last for 12 weeks and close during March 2019; this would allow enough period for stakeholders to respond. The Council was supportive of the proposed timetable in respect of this project.
- 10.3 In response to a query in relation to the matters to be taken into consideration in providing additional assurance on viability statement, it was agreed that the matter would be discussed at the Council Away Day in September 2018.

Data analytics and technology

- 10.4 The Council noted that audit firms had shared a number of concerns which the FRC needs to consider whether we need to take action to address them in respect of data analytics. The FRC had held a round table with representatives from a number of audit firms and developed a draft discussion paper to support wider stakeholder outreach and engagement.
- 10.5 The Council was supportive of the direction of travel to progress this project forward.
- 10.6 A Member outlined two-fold objectives of developing data analytics within firms: a) to enhance audit assurance and b) to create efficiency in delivering audit. The Member highlighted that data analytics probably creates high level of assurance but is more expensive than delivering reasonable assurance through the traditional way of auditing. The Council noted that the FRC's plan of action includes addressing some immediate needs with an intention to discuss at the IAASB level.
- 10.7 In response to a query in relation to the timeline of the project, it was reported that the intention is to continue the discussion with Council and provide an update on FRC outreach to Council at its meeting in September 2018.

Annual Quality Survey of audit Committee Chairs

- 10.8 The Council considered the annual survey questionnaire for audit committee chairs which seeks their views on audit quality based on the last audit cycle. The Council raised a query in respect of mind-set and culture and noted that the questions had not changed in the last three years. Whilst it was acknowledged that having consistent questions enables a clearer comparison from one year to another, the Council asked for reconsideration of the questions for next year to enhance overall insight. The results from the survey would be reported to the Council at its meeting in September 2018.

AQR Thematic Review – Other Information

- 10.9 The Council noted that the AQR is undertaking a thematic review of Other Information, to see how the audit firms have responded to the revised ISA (UK) 720. This will provide an opportunity to understand how audit firms are responding to an issue which is of increasing stakeholder interest and concern, and an early opportunity to see whether ISA (UK) 720 is achieving the outcomes that were intended when the standard was revised. The Council noted that the scope of the project has been approved by the Conduct Committee. The findings will be reported to the Conduct Committee in October with a tentative publication towards the end of the year. The Council agreed to discuss the outcome of the Review at a future meeting.

PN26 – Guidance on Smaller Entity Documentation

- 10.10 The Council agreed to recommend to the Codes & Standards Committee that it agree the proposal to withdraw the Practice Note 26 and issue a subscriber note to inform stakeholders. The rationale was explained as being that the practice note provides guidance to auditors on the documentation requirements for audit of financial statements of smaller entities, which are unlikely to be public interest entities and therefore not subject to the FRC's direct oversight and monitoring. The Council noted that the FRC will raise with the professional bodies the plans to withdraw the Practice Note, as it may be more appropriate for them to take forward responsibility for the development of this type of guidance in future.

SIR for Quantified Financial Benefits Statements

- 10.11 The Council noted that feedback to date from stakeholders was supportive of largely cosmetic updates to the current SIRs. The major market development since the last update were changes to the Takeover Code and introduction of Quantified Financial

Benefits Statements (QFBS). The Council noted that market practice has developed to deal with QFBS without regulatory intervention by the FRC. However, there is support amongst practitioners for the development of a new SIR (6000) to deal with QFBS engagements. In view of the growing need and the importance for these type of engagements, the Council was supportive of the view to develop a proposal and consult on a new SIR for QFBS.

11. Audit Quality Review Update

- 11.1 Mr Suffield provided an overview of the AQR work in the year. The work has two main objectives: holding UK audit firms that audit Public Interest Entities to account for the quality of their work, and underpinning the promotion of justifiable confidence in UK audit through evidence-based inspections. He summarised the:
- Ratings of the assessment of audit quality;
 - Inspection programme;
 - Results and key findings including reflections on inspections and concerns over results;
 - Key actions arising from the Review;
 - Thematic Reviews for the year 2017-18 and 2018-19.
- 11.2 It was queried whether AQR were raising the bar in terms of the standards they expect the firms to achieve. It was noted that the AQR seek to maintain a consistent approach in carrying out their inspections, providing appropriate challenge to audit teams. It was also noted that there was a strong working relationship between the AQR and the Audit & Assurance Team within the FRC which helps the AQR team to establish how well the standards were working in practice and provide feedback.
- 11.3 The meeting discussed the approach of the AQR team and the firms themselves in sharing insights to support continuous improvement. It was noted that AQR work in this area has developed well over the last couple of years, though the demands of competition limit the ability of the firms themselves to operate in this way.
- 11.4 The meeting also discussed how AQR inspection results compare to the inspection results of the ICAEW's QAD team who inspect non-PIE audits. The AQR Team compare the results of inspection with the QAD Team and noted that this year, with exception of one firm, the inspection results were broadly similar. Both teams share methodologies to bring about a better degree of alignment in the inspection process.
- 11.5 The Chair thanked Mr Suffield for his informative and useful update.

12. Any other business

FRC's response to IESBA's proposed strategy and plan 2019 - 2023

- 12.1 The Council considered the FRC's draft response to IESBA's proposed strategy and plan 2019 – 2023 and noted that the views expressed in the draft letter are consistent with the views expressed within the FRC's response to the IESBA's Strategy Survey in 2017. The Council had provided its views on the response to the Survey. The Council noted that three of the six top priorities identified by the FRC in the Survey were included in the proposed strategy and work plan, but the others had not made it to the final proposed plan and expressed disappointment. The Council was invited to provide their feedback on the FRC's draft response to the IESBA's proposed strategy and plan to Mr Babington by end of June 2018, to enable him to submit the response on time.

13. Date of next meeting

The next Council meeting would be held on 13 September 2018.