

TECHNICAL UPDATES

The Audit & Assurance Faculty roundup of new and updated legal and regulatory changes and guidance

AUDIT AND ASSURANCE
UK & IRELAND



DEVELOPMENTS IN AUDIT

October 2018

The Financial Reporting Council (FRC) has announced a strategic programme of work to ensure audit better serves the public interest. The programme, outlined in its report *Developments in Audit 2018*, covers work on auditor independence, audit quality, the future needs of investors and corporate viability.

The FRC will, as part of a comprehensive review of the 2016 auditing and ethical standards, test the effectiveness of the rules on independence. The review will determine whether further actions are needed to prevent auditor independence being compromised, including whether all consulting work for bodies they audit should be banned. The FRC will work closely with the Competition and Markets Authority (CMA) in this area.

Taking lessons from recent company failures, the FRC will develop proposals

to strengthen requirements on auditors when considering whether an organisation is a going concern. This includes whether the responsibilities of auditors in assessing companies' statements on their longer-term viability should be enhanced and whether auditors should report publicly on their views of the realism of assessments made by companies.

The FRC is undertaking a review of the work auditors do on the front half of the annual report to assess whether auditors are undertaking enough work to conclude it is not materially misstated. This will complement a major review of stakeholders' needs for information in corporate reports and will consider to what extent such information needs to be assured.

In the area of audit quality, the FRC has adopted an enhanced programme of audit firm monitoring. It has also strengthened its enforcement work so that it can conclude cases more quickly and revised its sanctions framework to levy penalties that reflect the gravity of the issue.

Developments in Audit 2018 is at tinyurl.com/AB-AuditDev

CMA REVIEW OF AUDIT

October 2018

The CMA has launched a detailed study of the audit sector to examine concerns that it is not working well for the economy or investors.

As part of its review, the CMA will investigate whether the sector is competitive and resilient enough to maintain high-quality standards.

The move comes amid growing concerns about statutory audits, in particular following the collapse of construction firm Carillion and the criticism of those charged with reviewing the organisation's books, as well as recent poor results from reviews of audit quality.

The CMA's market study will examine three main areas:

- Choice and switching. Changes put in place by the Competition Commission appear to have strengthened competition between the big four firms – Deloitte, KPMG, E&Y and PwC – but the largest UK companies still turn almost exclusively to one of them when selecting an auditor to review their books.
- Resilience. The market study will examine what the role of the big four firms means for resilience – the risk being that each of the big four auditors is “too big to fail”, potentially threatening long-term competition.
- Incentives. Companies, rather than their investors, pick their own auditor. The CMA's work will examine concerns that this might result in a lack of incentive to produce challenging performance reviews.

If the CMA finds evidence that the market is not working well after examining these areas, it will scrutinise all proposals for tackling them.

The CMA has written to the UK government about its market study and the possible need for legislation to implement its findings and those of the independent review of the FRC by Sir John Kingman.

The invitation to comment closed on 30 October 2018.

Responses and other information on the CMA's statutory audit market study are at tinyurl.com/AB-AuditStudy

FINANCIAL REPORTING UK & IRELAND



CORPORATE REPORTING AND GOVERNANCE

October 2018

In an open letter to finance directors and audit committee chairs, the FRC has called for improvements in key areas of corporate reporting. These include key accounting judgements and estimates, eliminating basic errors and how companies have applied the principles of the UK Corporate Governance Code.

The letter draws on findings from the FRC's *Annual Review of Corporate Governance and Reporting 2017/2018*.

The FRC reviewed 220 annual and interim reports for its 2017/18 monitoring activity and conducted three substantive thematic reviews on significant reporting issues.

Its key findings on corporate reporting were:

- The most significant concerns with financial statements included judgements and estimate disclosures and cash flow statements.
- Frequent challenges in the strategic report included the use of alternative performance measures and whether reports were fair, balanced and comprehensive.
- Viability statements have brought a greater focus on risk management but could be enhanced to show more clearly how companies have assessed their prospects and viability.

Its key findings on corporate governance were:

- Reported compliance with the Code is high. 95% of FTSE 350 companies reported they complied with all but one or two of the 55 provisions. However, reporting on how companies have applied the principles in the Code has been inadequately covered due to an excessive reliance on compliance with the provisions.
- Companies remained reluctant to explain clearly when they don't comply with the Code's provisions. The quality of explanations was described by FRC as disappointing. The FRC reiterated they must be thoughtful and provide a clear rationale for the action the company is taking.

A copy of the open letter to audit committee chairs and finance directors

is at tinyurl.com/AB-FRCLetter

The report *Annual Review of Corporate Governance and Reporting 2017/18* is at tinyurl.com/AB-FRCReview

RISK AND VIABILITY DISCLOSURES October 2018

Investors want companies to make business model, risk and viability disclosures more useful, according to a report from the FRC's Financial Reporting Lab.

Business model reporting; Risk and viability reporting - Where are we now? considers how reporting practice has changed since the lab published its reports in 2016 and 2017. The report includes practical examples from companies that have implemented the recommendations in those reports.

The report is at tinyurl.com/AB-LABReport

FUTURE OF CORPORATE REPORTING (October 2018)

The FRC has launched a project to challenge existing thinking about corporate reporting and consider how companies should better meet the information needs of shareholders and other stakeholders. It will review current financial and non-financial reporting practices, consider what information investors and other stakeholders require and the purpose of corporate reporting and the annual report. The different types of corporate communications produced by companies will also be examined.

Ideas and suggestions on how corporate reporting should evolve can be sent to futurereporting@frc.org.uk

The FRC expects the project to lead to calls for action on changes to regulation and practice. During the second half of 2019, the FRC will publish a thought leadership paper consolidating the outcomes of the project.

Learn more at tinyurl.com/AB-CorRep

REVISED TAXONOMIES October 2018

The FRC has amended its suite of taxonomies, which were last issued in December 2017.

The latest taxonomy suite covers

International Financial Reporting Standards (IFRS) that have been endorsed since the 2018 taxonomy suite releases, including IFRS 9 *Financial Instruments*, IFRS 15 *Revenue from Contracts with Customers* and IFRS 16 *Leases*. It also reflects Triennial Review amendments made to UK GAAP standards in December 2017.

The taxonomies are effective from 1 January 2019, with early adoption permitted.

Further information is at tinyurl.com/AB-Taxonomies

AUDIT AND ASSURANCE CROWN DEPENDENCIES



CONSULTATION ON AUDIT RULES October 2018

The three oversight bodies of Jersey, Guernsey and the Isle of Man have launched a new consultation on the Crown Dependencies Audit Rules.

Affected firms are encouraged to respond before the 19 December deadline. The new regulations are expected to take effect from 6 April 2019.

Earlier in 2018, an updated version of the Crown Dependency Audit Rules and Guidance was proposed. In response, a number of firms directly contacted the oversight bodies and requested that implementation be delayed until the implications of their scope were fully considered and explained. A particular area of concern is the extension of the definition of public interest entities to include all Market Traded Entities.

This led to the proposed new regulations being stood down and the Crown Dependencies Audit Rules (2015) continue to apply.

The consultation paper is at tinyurl.com/AB-CrownConsult

AUDIT AND ASSURANCE INTERNATIONAL



ISA 540 REVISED
October 2018

The International Auditing and Assurance Standards Board (IAASB) has released International Standard on Auditing (ISA) 540 (Revised) *Auditing Accounting Estimates and Related Disclosures*.

ISA 540 (Revised) reflects the rapid change that banks, insurers and other financial services firms have seen as they moved to new accounting standards that have changed the way they deal with loan provisions and insurance contracts.

Some of the significant revisions include:

- An enhanced risk assessment that requires auditors to consider complexity, subjectivity and other inherent risk factors in addition to estimating uncertainty. The aim is to drive auditors to think more deeply about the risks inherent to accounting estimates.
- A closer link between the enhanced risk assessment and the methods, data and assumptions used in making accounting estimates, including the use of complex models.
- Specific material to show how the standard is scalable to all types of accounting estimates.
- Emphasis on the importance of applying appropriate professional scepticism when auditing accounting estimates to foster a more independent and challenging mindset in auditors.

ISA 540 (Revised) is effective for financial statement audits for periods beginning on or after 15 December 2019 and is available at tinyurl.com/AB-ISA540-Rev

PROFESSIONAL SCEPTICISM
October 2018

The IAASB has published its first update to stakeholders, highlighting its efforts to reflect professional scepticism in its standards.

The update, titled *Professional Scepticism Communiqué*, is available at tinyurl.com/AB-PSUpdate

INTERNATIONAL FEDERATION OF ACCOUNTANTS



DRIVERS OF SMP GROWTH
October 2018

Accountants working in small and medium-sized practices (SMPs) are embracing technology to better serve clients and attract and retain top talent, according to the International Federation of Accountants (IFAC) *2018 IFAC Global SMP Survey*.

IFAC received more than 6,000 responses from SMPs, representing 150 countries, about their performance in 2018 and marketplace factors most likely to affect them in the future.

The survey found that over a quarter of SMPs (28%) plan to allocate more than 10% of practice revenue over the next year to technology investment, reflecting its critical importance in practice management and operations.

The most frequent responses to technological advances have been the development of in-house expertise in IT and the adoption and use of cloud options to better serve clients.

The survey is at tinyurl.com/AB-SMPSurvey

GLOBAL STANDARDS ADOPTION
October 2018

The implementation of transparent and high-quality international standards is improving the availability of high-quality financial information for stakeholders, investors and the public, according to a new report from IFAC.

The *International Standards: 2017 Global Status Report* is the first of its kind to provide information that has been collected through the IFAC Member Compliance Programme.

The programme measures progress in adopting international standards and highlights the essential role they are playing in strengthening economies.

A copy of the report is available at tinyurl.com/AB-AWBReport

ACCOUNTANCY EUROPE



IMPLEMENTATION UPDATE ON EU AUDIT RULES
October 2018

Accountancy Europe has published an update on the state of play of European Union (EU) Member States' implementation of new EU audit rules. More information on the process is available at tinyurl.com/AB-EUAuditRules

ICAEW



BREXIT GUIDANCE
November 2018

ICAEW's technical strategy department has issued a Brexit guide on *Recognition of professional qualifications*. It covers:

- the current situation for ICAEW members in the UK and EU27;
- arrangements if there is a withdrawal agreement and a transition period;
- implications of a 'no deal' scenario for ICAEW members pursuing new recognition applications;
- implications of a 'no deal' scenario for EU professionals pursuing new recognition applications in the UK, and with ICAEW specifically;
- implications for students; and
- what ICAEW is doing to engage with the UK government and the EU institutions during the negotiation process.

Download the guide at tinyurl.com/AB-Brex ●



Peter Mandich produces Technical Updates. He is a manager in the Audit & Assurance Faculty