

Annual General Meeting of the Audit Committee Chairs' Independent Forum

Wednesday 18th December 2019

Summary of activities during 2019 (in chronological order)

Member panel event

On **31 January 2019**, the Audit Committee Chairs' Independent Forum held an event to discuss the following three reviews:

- CMA – Statutory audit services market study – Update paper
- Kingman - Independent Review of the Financial Reporting Council
- Launch of the Brydon Review (including the expectation gap findings from the CMA inquiry)

The discussion focused on three specific elements of the debate:

- The expectation gap
- Audit committee accountability
- Joint audit

The discussion was led by a panel made up of representatives from the Audit Committee Chair, CFO, Investor and Auditor community.

A summary of the event is available from

http://www.accif.co.uk/accif_full_note_of_31_Jan_2019_event.pdf

Roundtable with the Investment Association

On **29 May 2019**, a group of ACCIF members attended a roundtable with members of the Investment Association to discuss effective engagement practices between audit committees and the investor community.

Independent Review of the Financial Reporting Council – Initial consultation on the recommendations

On **5 June 2019**, submitted a response to BEIS on its initial consultation on the recommendations of the Independent Review of the Financial Reporting Council. At the same time, we issued a joint response with the FTSE 100 CFO community. Given the roles of both CFOs and Audit Committee Chairs in the front line of corporate reporting and auditing, we considered it would be beneficial to collaborate on some key recommendations which we believe are workable and could have impact.

In our response ACCIF was supportive of the recommendations made in relation to the following three areas.

1. A strengthened framework around internal controls in the UK
2. An effective enforcement regime in relation to PIEs that holds relevant directors to account for clearly defined duties
3. Going concern and longer term viability statements

In addition, we took the opportunity to make the ACCIF position on mandatory joint audit clear. Audit quality is absolutely fundamental for audit committee chairs. ACCIF has seen no evidence that imposing mandatory joint audits with a firm outside the Big 4 will have a positive impact on audit quality and, in fact, it is believed that this could well have the opposite effect.

The full letter is available here http://www.accif.co.uk/ACCIF_BEIS%20response_signed_050619.pdf

Independent Review into the quality and effectiveness of audit – Call for views

On **7 June 2019**, ACCIF submitted a response to the Brydon Review team. Here is a high level summary of the key points made in ACCIF's response to the Brydon Review. The full letter is available here <http://www.accif.co.uk/ACCIFresponseToBrydon.pdf> :

Definitions of audit and its users - any requirements for independent assurance of information outside the financial statements should be set quite separately from the audit of financial statements and not seen as an extension of that audit.

The 'expectation gap' - the key issue to address is the extent to which it is reasonable to expect auditors to be able to provide greater assurance on matters relating to the future viability of companies and on the prevention and detection of corporate fraud. This cannot be done without first determining exactly what directors should be required to report in relation to these matters, and then to assess the extent to which it is practicable to require auditors to provide assurance regarding the statements made by directors.

Risk and internal controls – we support the introduction of a requirement for directors to report on their assessment of the effectiveness of the entity's system of internal control relevant to risks that may affect financial reporting and for the (external) auditors to attest to and report on the directors' assessment.

Going concern - in order to give greater emphasis to the requirements underlying the going concern statement, consideration could be given to requiring the statement to include a specific confirmation by the directors that in their view there are no material uncertainties relating to events or conditions that might cast significant doubt upon the continuing use of the going concern basis of accounting in future periods.

Viability – the focus of the viability statement should be to highlight the potential impact of risk on the sustainability of the business model. It is likely that the most that can realistically be achieved for the viability statement is a statement by the directors of all the key assumptions on which the statement is based. Assurance on the completeness of the stated assumptions might be possible to obtain but nothing more.

Audit quality - looking forward, and with an eye to the likely increasing use of technology, thought should be given to identifying the drivers that underpin the delivery of quality and the market participants' investment in these. The Audit Firm Transparency Reports should provide greater transparency on the profitability of the audit businesses, their investment in quality drivers and their ability to sustain these over time. The independent board members of the audit firms have a key role to play in promoting and ensuring transparency and building public confidence in the auditing profession.

Audit reporting - it has been suggested that where there is significant measurement uncertainty, auditors should also indicate how conservative or aggressive they believe the assumptions and judgements applied by the directors to be. In our opinion, the starting point is for the directors to disclose the sensitivities associated with particular items in the accounts. Where this is done, auditors should then be able to comment in their report on the range of possible outcomes and the directors' rationale for the point in the range they have applied.

Investor (and stakeholder) engagement – it is critical that this review considers the effectiveness of engagement and how this can be improved and sustained. Audit and risk are far more critical to the value of the investment, yet the resource committed is minimal by comparison to that dedicated to remuneration matters.

Meeting with the EY Independent Non-executives

On **25 June 2019**, members of ACCIF were invited to a meeting with the EY Independent Non-executives to discuss EY's approach to audit quality. In 2020, the intention is to meet with the INEs of the major audit firms and also to do a follow-up session with the EY INEs.

Roundtable with Sir Donald Brydon and the Brydon Review Secretariat

On **10 July 2019**, members of ACCIF attended a roundtable with Sir Donald Brydon to provide some additional input to the review and also to discuss the contents of our submission in more detail.

Roundtable with BEIS officials on the CMA recommendations

On **3 September 2019**, members of ACCIF attended a roundtable with the BEIS officials responsible for the Government's response to the CMA recommendations, e.g. in relation to mandatory joint audit, operational split of the audit firms and enhanced scrutiny of audit committees. This discussion was used to develop our formal response to BEIS (see item below).

Market Study on Statutory Audit Services – Initial consultation on recommendations by the CMA

On **19 September 2019**, ACCIF submitted a response to BEIS on its initial consultation on recommendations by the CMA. ACCIF's key points are set out below:

ACCIF is keen to see a solution to choice but not at any cost. We want to work with change that is measured and will not put quality at risk. There were three aspects in particular which ACCIF highlighted. These are:

Big 4 v non-Big 4 auditor selection - there is a perception that there is an unfounded bias against the selection of non-Big 4 auditors; the audit committee chairs, not surprisingly, don't subscribe to this, however are interested in how to address this through enhanced communication around selection and other means.

Capacity in the market - as discussed in our meeting, Audit Committee Chairs support increased choice; they are however, very concerned that a path to change is selected that is out of step with the market that we have to select from. There needs to be confidence for stakeholders that change has a high chance of success and has the support of those taking responsibility for its operation.

Understanding the market – linked to the point above, the Audit Committee Chairs feel strongly that there has yet to be a detailed analysis of the characteristics of the FTSE 350 such that an informed decision can be made in relation to where the complexity lies and, therefore, where more specialist and experienced audit provision will be required. We feel it is too simplistic to work on the assumption that FTSE 100 is complex and the lower end of the FTSE 350 is more straightforward. There needs to be consideration of factors such as geographical locations, regulation, industry specialisms, use of shared service centres etc.

Meeting with analysts to discuss their use of corporate reporting

On **9 October 2019**, representatives of ACCIF met with a leading analyst firm to understand their perspectives on a number of corporate reporting matters including length and readability; their key areas of focus and practices which aid effective communication. Following this meeting a further submission was sent to the Brydon Review Team to draw out some of the points raised. These included points on the timing and content of the preliminary announcement and also a lack of consistency in financial reporting.

Joint meeting with CBI & Hundred Group and BEIS officials

On **10 October 2019**, representatives of ACCIF joined with counterparts from the CBI and the Hundred Group at a meeting with BEIS officials to discuss more detail around the CMA recommendations. An outcome of this session was that ACCIF agreed to survey members in relation to their recent experiences of tendering and the challenger firms. We also asked members for their views on the complexity of the audit market and what characteristics drive that complexity. We received over 35 responses to our survey and these responses have been summarised, anonymised and shared with BEIS. The results show that there is a high level of consistency between those characteristics of complexity and the reasons for challenger firms either choosing not to tender for an audit or for not being selected. The results further demonstrated that, based on our respondents across a range of company sizes, there was no evidence of bias towards the Big 4 audit firms. These characteristics are as follows:

- Geographical location(s)
- Number of locations
- Regulated industry
- Tax and other fiscal arrangements
- Industry-specific complex transactions
- Specific risks, e.g. technology, cyber, complex financial instruments etc
- In depth expertise in sector or other specialisms
- Level of IT reliance
- Structural complexity - ownership and control

Response to the IIA on a draft Code of Practice for Internal Audit

On **11 October 2019**, following a meeting of some members, ACCIF submitted a response to the IIA in relation to their draft Code of Practice for Internal Audit. ACCIF has a keen interest in having a robust and effective internal audit function and believes that there is much in the draft Code of Practice which cannot be argued with. So that the Code is taken seriously, ACCIF believes it is important to recognise that there will be different models applied in order to satisfy the key principles. It needs to be recognised that it will not be appropriate for many companies to hire the level of internal audit head envisaged in the code. It needs to be left to the judgement of the Audit Committee Chair to approve the resourcing model that a particular business requires.

Second Investment Association roundtable

On **22 October 2019**, a group of ACCIF members attended a second roundtable with members of the Investment Association to discuss effective engagement practices between audit committees and the investor community. This session focused more specifically on audit committee communication with investors and a number of existing practices were discussed, e.g. audit committee attendance at analyst presentations and/or governance days. A series of investor 'training' workshops were also discussed as an aid to better understanding of audit committee matters.

Looking ahead to 2020

There will continue to be much for ACCIF to focus on and respond to:

- Sir Donald Brydon's report on the quality and effectiveness of audit
- BEIS consultations on the Kingman and CMA recommendations
- The audit committee's role in relation to addressing the impact of climate change
- Facilitating more effective engagement with investors
- Implementation of the new Ethical Standard and the auditing standard on going concern