Association of International Certified Professional Accountants

The Helicon, One South Place, London EC2M 2RB, United Kingdom

T: +44 (0) 20 7663 544

aicpaglobal.com | cimaglobal.com | aicpa.org | cgma.org

Rt Hon. Kwasi Kwarteng MP
Secretary of State
Department for Business, Energy and Industrial Strategy
1 Victoria Street
London
SW1H 0ET

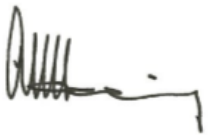
7 July 2021

Dear Secretary of State,

Please find below the Association of International Certified Professional Accountants response to the Department for Business, Energy and Industrial Strategy consultation on the Restoring Trust in Audit and Corporate Governance White Paper.

Thank you for the opportunity to respond.

Yours sincerely,



Andrew Harding
Chief Executive - Management Accounting
Secretary General, CIMA

About the Association

The Association of International Certified Professional Accountants® (the Association), representing AICPA® & CIMA®, advances the global accounting and finance profession through its work on behalf of 696,000 AICPA and CIMA members, students and engaged professionals in 192 countries and territories. Together, we are the worldwide leader on public and management accounting issues through advocacy, support for the CPA license, the CGMA designation and specialised credentials, professional education and thought leadership. We build trust by empowering our members and engaged professionals with the knowledge and opportunities to be leaders in broadening prosperity for a more inclusive, sustainable and resilient future.

The American Institute of CPAs® (AICPA), the world's largest member association representing the CPA profession, sets ethical standards for its members and U.S. auditing standards for private companies, not-for-profit organisations, and federal, state and local governments. It also develops and grades the Uniform CPA Examination and builds the pipeline of future talent for the public accounting profession.

The Chartered Institute of Management Accountants® (CIMA) is the world's leading and largest professional body of management accountants. CIMA works closely with employers and sponsors leading-edge research, constantly updating its professional qualification and professional experience requirements to ensure it remains the employer's choice when recruiting financially trained business leaders.

Contact

For further information about the Association and its submission, please contact Ross Archer, Lead Manager – Public Policy at ross.archer@aicpa-cima.com.

Association of International Certified Professional Accountants®

General Comments

The Association of International Certified Professional Accountants (Association), either as CIMA or as the AICPA, has responded to every consultation the UK Government have brought forward on the issue of audit and corporate governance reform in the UK over the last few years.

These include the Wates Review, the Sir John Kingman Review, the CMA Audit Market Study and the Sir Donald Brydon Review. We welcome this further opportunity to respond to what the government is proposing following these reviews in their White Paper titled Restoring Trust in Audit and Corporate Governance.

Below are some general comments on the key themes and proposals the White Paper puts forward and we have responded to individual questions further below.

PIEs

We support extending the number of Public Interest Entities in the United Kingdom. We have suggested that this could be achieved by using tests that look at a range of factors including UK based employees, size of turnover and profits. Any company registered and listed on AIM should be considered a PIE.

We do not agree with pausing or delaying aspects of the reforms for newly listed PIEs or limiting them to premium listed PIEs. If an entity has been classified a PIE it is likely to impact the public interest in the same way as any other PIE and therefore, they should all be subject to the same standards and reforms.

Internal Control

The Government could have gone further with its proposed reforms around internal controls at entities. We would have liked to see the Government introduce more robust requirements with respect to internal control than they have proposed. Such requirements may be along the lines of section 404 of the Sarbanes Oxley Act in the United States in which the management of public companies are required to assess the effectiveness of internal control over financial reporting and the public company's auditor is required to attest to, and report on management's assertion of its internal control. An introduction of something similar to the Sarbanes Oxley internal control requirements would lead to enhanced financial reporting and greater transparency of internal control within PIEs.

Resilience Statement

The introduction of a Resilience Statement that sets out a company's approach to exploring and mitigating risks and uncertainties over the short-term, medium-term, and longer-term we believe will help both investors, shareholders and wider stakeholders assess, to a greater level than is current, how resilient the business is and how prepared they are for future challenges.

Audit and Assurance Policy

We welcome the introduction of an Audit and Assurance Policy and agree it should be three year rolling and put to an annual advisory vote by shareholders for approval at the Annual General Meeting.

Public Interest Statement

The Government should introduce a Public Interest Statement. Such a statement would provide an opportunity for directors to articulate in a holistic way how the company they govern serves the wider public interest and give an explanation by the directors of how they perceive the public interest in their company, and how they have taken measures to serve that interest over the previous year. This statement could help to inform shareholders decisions in respect of where they invest and the scrutiny they provide.

True and Fair

We are disappointed that the government have decided not to follow the Brydon recommendations to replace the 'true and fair' wording in the Companies Act 2006 with "present fairly, in all material respects".

Fraud

A holistic approach to fighting fraud is needed that involves directors, management, internal auditors, and external auditors. The proposal to require directors of Public Interest Entities to report on the steps they have taken to prevent and detect material fraud we support.

We also support improving education on fraud and the creation of a fraud register run by the regulator.

While auditors could provide assurance on the proposed director's statement regarding actions taken to prevent and detect fraud, it would be more effective for auditors to evaluate all of internal control over financial reporting (not just those controls/actions to prevent and detect fraud). Further, it should be noted that such an engagement would be beyond that performed in an audit of financial statements and there may be reporting implications that would need to be considered (for example, would the auditor issue one report that addresses the financial statement audit and the assurance engagement on the director's statement or would two separate reports be issued).

If auditors are required to report on directors of PIEs effectiveness of relevant controls to stop fraud, then what these relevant controls that auditors are required to report on needs to be more clearly defined before this proposal is implemented.

Operational Split

We still have concerns around the operational split proposals for the Big 4 audit firms and do not think they will deliver the results that are intended. We think these proposals could harm the quality of audits provided; lead to less skilled auditors; lack of access to specialists; lack of investment in audit technology; increased audit costs and potentially firms leaving the audit market.

However, we do note that the Big 4 in the UK have entered a voluntary arrangement to operationally split.

Managed Shared Audit and Market Share Cap

Managed Shared Audits will lead to several challenges, and we do not believe will lead to changes that impact competition. For example, we think some consequences of this requirement include

disincentivising innovation, and higher audit costs. Further, this approach still does not address that some 'challenger' firms lack capacity or experience to engage in PIE audits. It also does not take into account the multi-national nature of PIEs.

We do not support the introduction of a Market Share Cap and believe this proposal if introduced would harm the quality of audits provided.

Regulator Power to Appoint Auditors

We are concerned around the proposals to give the regulator power to appoint auditors of PIEs. An entity should have the freedom to appoint their own auditor. Further, if a PIE is unable to hire an auditor on their own, this generally is due to underlying issues present at the PIE. Where an auditor does not wish to conduct an audit of an entity they should not be forced to do so.

New Professional Body for Auditors

We do not agree that a new professional body for auditors will result in better quality of auditors and higher quality audits in future. We think the government needs to consider this idea carefully before proceeding and we explain why in our answers to the specific questions on this.

Audit Reporting and Governance Authority (ARGA)

The proposed objective of ARGA in this White Paper is more broadly defined than in the Sir John Kingman review. We think it is unhelpful that the new definition de-emphasises the importance of ensuring adequate standards in audit, corporate reporting and corporate governance that the Kingman Review identified.

We believe a key aim of ARGA must be to regulate the entire boardroom, rather than only those directors who happen to be professionally qualified.

We do not see the evidence that justifies requiring the chartered bodies to comply with ARGA oversight via legislation. All the chartered bodies have worked effectively with the FRC under existing arrangements and do not see why this would not continue. We are concerned that this will impose a further and expensive layer of regulation on the chartered bodies and be funded by them and their members, which could disincentivise membership, with all the benefits that proper qualifications and professional regulation offers in the public interest.

We do not agree that the regulators enforcement powers should only apply to members of professional accounting bodies. This risks lessening the incentives to become members of the professional bodies and if the regulator is there to regulate the whole market it should not be restricted to just one element of it.

Reforms Won't Stop Corporate Failure

Enterprises fail regularly. Even large enterprises and public companies fail. There is a danger of conflating corporate failure with audit failure when the two are not synonymous.

In most corporate failures there are many factors that contribute to the ultimate demise of the enterprise. These relate to external as well as internal pressures on the organisation. There are always lessons to be learned from failure and these disruptions can lead to increased innovation.

We are concerned that some see all corporate failure as due to poor audit or regulation. This is not the case. Not all businesses succeed; this is the nature of business. Business operates with risk and

sometimes that involves failure. These reforms should not be seen as eliminating that risk or attempting to stop corporate failure, as no amount of reform of the audit market would accomplish that.

Association of International Certified Professional Accountants

Answers to Specific Questions

1. **Should large private companies be included within the definition of a Public Interest Entity (PIE)? Please give your reasons.**

   We do agree that the number of PIEs should be expanded to include companies who have a significant impact on the public interest and matter to a range of stakeholders.

   Companies that are not already defined as PIEs can have significant effects on a range of different stakeholders and investors and ensuring they have the highest reporting, auditing and corporate governance structures will help maintain confidence in them and the services they provide. However, there should be a clear test and definition as to what is a PIE that we seek to answer in Question 2.

2. **What large private companies would you include in the PIE definition: Option 1, Option 2 or another? Please give your reasons.**

   Any move to include more companies as PIEs for the purposes of reporting and auditing should align with the UK Companies Act.

   Some jurisdictions use a Public Interest Scorecard to help define who would be classified as a PIE with points given for size of turnover, profits, number of employees, etc… The government may wish to explore these models so every company can understand in future if they have reached the threshold to become a PIE.

   In the EU a PIE is defined in law as large companies having over 500 employees. We would recommend any future UK definition taking into account the size of a company's employees and feel that the definition of a PIE should include companies that have over 500 UK based employees. Such an employee threshold brings in a wide range of businesses. It ensures that a key stakeholder group is not marginalized.

   We would also suggest a test which includes turnover in addition to employees regardless of whether the entity issues shares on a regulated market. This may be justified as larger businesses are increasingly employing less people while still having large societal impacts. The government should review what turnover tests for PIE definitions are in place across the world before adjusting the threshold in the UK.

   Furthermore, the review should consider how the size test may be avoided by some entities. This could be done by an entity restructuring which will potentially introduce complexity and inefficiency into the corporate structure or lead companies to relocate some activities out of the UK which is not in the best interests for UK society.

   We feel that the public interest test should ensure that any company listed on either the FTSE 350 or AIM are included.

3. **Should AIM companies with market capitalisation exceeding €200m be included in the definition of a PIE? Please give your reasons.**

   Please see answer to Question 1 and 2.

4. **Should Government give newly listed companies a temporary exemption from some of the new reporting and attestation requirements being considered for Public Interest Entities?**

   No. Newly listed companies are likely to impact the public interest in the same way as others and should start as they intend to continue.

6. **Should the Government seek to include large third sector entities as PIEs beyond those that would already be included in the definitions proposed for large companies? If so, what types of third sector entities do you believe should be included and why?**

   Please see answer to Question 1.

7. **What threshold for 'incoming resources' would you propose for the definition of 'large' for third sector entities? Is exceeding £100m too high, too low or just right? £100m seems to high and the limit should be comparable to that of other similarly sized organisations.**

   £100m seems too high and the limit should be comparable to that of other similarly sized organisations.

8. **Should any other types of entity be classed as PIEs? Why should those entities be included?**

   Please see answer to Question 1 and 2.

9. **How would an increase in the number of PIEs impact on the number of auditors operating in the PIE audit market?**

   We think that an increase in the number of PIEs will mean an increase in the number of audit firms providing audit services to these entities. This is as the market grows in PIEs it could mean that challenger audit firms can get more access and experience in auditing larger companies as they can tender for more PIE audits.

   According to the FRC 2019 audit report those companies listed on AIM the Big Four only has audit accounts for 32.6% while other audit firms have 67.4% of the AIM market audits. This would suggest that as the number of PIEs grow so too will the number of audit firms outside of the Big Four conducting these audits.

   This could also mean as PIE firms take on audit firms outside of the Big Four and these firms gain experience and resources for doing these kind of audits, more and more PIE firms will consider taking on audit firms outside of the Big Four and thus increasing competition and resilience in the audit market.

10. Do you agree that the Government should provide time for companies to prepare for the introduction of a new definition of PIE?

The Government should always ensure adequate time to prepare for major legislative change and set out a clear timeline for companies to prepare for changes. However, all PIEs should be subject to any reforms at the same time as they are likely to impact the public interest in the same way as others.

11. Do you agree that the Government should seek to offer a phased introduction for a new definition of PIE?

A clear timeline for companies to prepare for these changes would be welcome, but as we answered in Question 4 and 10 all PIEs should be subject to changes at the same time.

12. Is there a case for strengthening the internal control framework for UK companies? What would you see as the principal benefits and disbenefits of stronger regulation of internal controls?

There is a case for using the framework of internal control provided by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) Internal Control-Integrated Framework (ICIF) (the "COSO Framework") This framework is globally regarded and widely used and so merits consideration in being used here in the UK.

Any move to a rules-based approach on internal controls should take account of the UK's traditional principles-based approach to internal control. There is undoubtedly an additional cost to introducing regulatory burden that needs consideration.

13. If the control framework were to be strengthened, would you support the Government's initial preferred option (Table 2)? Are there other options that you think Government should consider? Should external audit and assurance of the internal controls be mandatory?

We think that requiring an explicit directors' statement acknowledging their responsibility for oversight of internal control, requiring directors to carry out an annual review of the effectiveness of internal control, then explaining the outcome of that review and whether they consider the systems to have operated effectively, and explaining how they have assured themselves of the appropriateness of that statement would help improve transparency and investors' knowledge. We believe this would support better investment as investors would understand the director's responsibility regarding the controls within the entity in which they have invested. Also, we believe that such a statement would enable better scrutiny by boards of directors.

We think a directors' statement on the effectiveness of internal control as proposed in Option A should be introduced. If such statements by directors are introduced, we believe it should be on a statutory footing, as this would mean more entities are brought under its scope and a greater likelihood of enforcement than if it were introduced under the UK Corporate Governance Code. Such a statement should apply to all PIEs and not just to those that are premium listed. It makes little sense to bring more PIEs into scope for all the other reforms outlined in this White Paper, and not to include them in this aspect.

We believe that in the event that false or misleading statements are made, were Option A to be introduced, the makers of those statements should face enforcement action as outlined in Chapter 5 of this White Paper.

The consultation paper proposes that the COSO Framework adapted for the UK could be used for assessing the effectiveness of the internal controls for financial reporting. We support this. The COSO Framework is used around the globe and is widely accepted as the most comprehensive principles-based internal control framework. The COSO Framework covers five components (Control Environment, Risk Assessment, Control Activities, Information & Communication and monitoring) and provides 17 principles covering those five areas regarding internal control and guidance regarding the design and implementation of the principles. As an example, the COSO Framework is used by issuers in the U.S. to assess their internal control as well as auditors in evaluating a company's internal control. The concepts in the COSO Framework could easily be applied in the UK.

If the government wants to improve internal controls within PIEs while introducing Option A, they must also introduce Option C alongside it.

If a directors' statement on whether they consider the systems to have operated effectively (and an explanation of the basis for that statement) is introduced, it would provide boards and shareholders with more confidence in the entity if this statement was subjected to an assurance service by the entity's financial statement auditors.

We recognise this would be similar to section 404(b) of the Sarbanes Oxley legislation in place in the USA.

In the US, the Sarbanes-Oxley Act of 2002 (SOX) section 404 (a) requires that the management of public companies assess the effectiveness of the internal control of issuers for financial reporting. SOX Section 404(b) requires a publicly held company's auditor to attest to, and report on, management's assessment of its internal controls. Subsequent rulemaking in the US has made Section 404(b) applicable to a certain subset of issuers.

Sections 404(a) and 404(b) have led to improved financial reporting and greater transparency regarding the effectiveness of internal control. Because of the significant benefit to investors, the Association supports the implementation of something that resembles SOX section 404 (a) and 404(b) for all publicly traded companies and opposes exemptions from the provision. We believe that all investors in public companies should have equal benefit of the same protections. Some small companies have argued that the regulatory cost and burden of having the assessment outweighs the benefit to investors.

Importantly, the US Government Accountability Office has found that - since the implementation of the auditor attestation requirement of SOX, companies exempt from the requirement have had more financial restatements (a company's revision of publicly reported financial information) than non-exempt companies, and the percentage of exempt companies restating generally has

exceeded that of non-exempt companies[1]. Exempt and non-exempt companies restated their financial statements for similar reasons (e.g., revenue recognition and expenses), and the majority of these restatements produced a negative effect on the companies' financial statements.

As regards what an auditor would attest to in relation to the directors' statement on internal controls, this will need to be clearly defined in order that boards and shareholders understand the assurance provided by the statement. In the US it is very narrowly defined and focuses on internal control over financial reporting. If broader criteria were included, this could add to audit costs.

We think that the attestation of the statement should be in line with the frequency of the directors' statement. For both we think that an annual statement and attestation would be the best approach and would be in line with the US and what is working there.

Based on the above, we do not believe what the government has set out in the preferred options in Table 2 goes far enough. We believe that if this is the limit of what is introduced, while it will be an improvement on the current internal control and reporting landscape, issues will still remain.

In particular, we think that the directors' statement on internal controls should be separate to the annual report. This would highlight the importance of this report to both the board and investors. We also think that by requiring only the statement as to whether they consider the systems to have operated effectively without related external assurance will mean that the changes in this area are not as effective as they could be. If these statements are regularly assured then potential issues and poor internal controls can be spotted and dealt with sooner, thus providing better corporate governance and a better and more informed landscape for investors.

As we have said in previous questions, we think any changes in these areas should apply to all PIEs straight away and not just after two years.

14. If the framework were to be strengthened, which types of company should be within scope of the new requirements?

As we have answered in previous questions, we believe that all PIEs should be within scope. In answer to Question 13 we give an example in the US that shows that those entities that are part of the Sarbanes Oxley internal controls process have fewer financial restatements than those that are exempt from it.

19. Do you agree that the above matters should be included by all companies in the Resilience Statement? If so, should they be addressed in the short or medium term sections of the Statement, or both? Should any other matters be addressed by all companies in the short and medium term sections of the Resilience Statement?

We welcome the government agreeing with the Brydon Review that PIEs should publish an annual Resilience Statement that sets out a company's approach to exploring and mitigating risks and uncertainties over the short-term, medium-term, and longer-term.

[1] https://www.gao.gov/products/gao-13-582

The experience of the pandemic has showed how important resilience is for businesses of all sizes and across all sectors. We believe that an annual Resilience Statement by PIEs will help investors, shareholders and wider stakeholders assess to a greater level than is current how resilient the business is and how prepared they are for future challenges.

Our observation is that companies which have demonstrated good practice in the area of Viability Statements have focused on providing high-quality information on the underlying process and scenarios which have underpinned the resulting viability statement – in effect, 'showing they're working'. We suggest that directors are as part of the Resilience Statement asked to address their risks and opportunities in the context of a company's business model. This should be focused upon how value is currently created, and the basis for the creation of value in the future for investors and those stakeholders material to the company.

We agree with a five-year reporting period for the medium-term section of the statement instead of the three years currently required by Viability Statements. We think this change will identify more potential risks that will help better inform stakeholders, investors, shareholders and the company itself as to how these can be mitigated.

We also welcome the proposals that more scenario planning should play a role in the Resilience Statement. Scenario planning is a key activity that needs encouragement both in core viability but could also encourage a cultural change and better understanding of risk.

Management Accountants will play a key role in performing the scenario tests that are part of the proposed statement. We would welcome greater Management Accounting involvement in helping with, testing and reporting on the resilience of the entity via the Resilience Statement to the benefit of all stakeholders.

We agree with the areas identified by the government to be included within the Resilience Statement and especially supply chain risk. We also welcome the climate change risk proposal, and the government may wish to explore whether wider sustainability considerations may be more appropriate for the proposed statement. Other risks could also be included such as regulatory risks, natural resources, cyber risks, talent risks or people risks.

There may also be a case for shareholders to be able to exert some influence over what a PIE, in which they have invested, includes as a risk in its Resilience Statement. Some PIEs may be involved in more risk-based sectors or have different and unique risks compared to others and to ensure good corporate governance should report on these risks above the minimum risks set out by the government in this consultation. However, thought should be given so that shareholders could not automatically demand an area to be included in the statement. Instead the company directors should consult shareholders ahead of preparing the statement, so that views can be sought on the areas to be covered by the Resilience Statement.

The question of legal safe harbours may need to be considered in relation to the Resilience Statement, and this issue should be explored in the government's forthcoming consultation.

We welcome the commitment to further consultation on this area and think it is right that the government considers this in greater detail in order to ensure the Resilience Statement is both useful to the entity, shareholders and wider entity stakeholders and drives better corporate decision making.

20. Should the Resilience Statement be a vehicle for TCFD reporting in whole or part?

We believe the Resilience Statement should in part be a vehicle for TCFD reporting. At the very least it should in our view refer to a climate change scenario analysis of a 2 degrees C increase scenario and its impact on an organisation. This should be in terms of the long-term challenges to the organisation and its business model.

However, with the June 2021 launch of the Taskforce on Nature-related Financial Disclosures (TNFD) and its forthcoming framework, the Resilience Statement going forward should consider and disclosure both nature and climate jointly.

21. Do you agree with the proposed company coverage for the Resilience Statement, and the proposal to delay the introduction of the Statement in respect of non-premium listed PIEs for two years? Should recently-listed companies be out of scope?

We believe there should be a clear timeline for all PIEs to comply with the introduction of the Resilience Statement. PIEs should be encouraged to produce Statements even before they are legally required, to ensure the highest possible standard of reporting.

We do not agree that recently listed companies should have a grace period before being required to produce a Statement. There should be a clear deadline indicating when a newly listed company has to start to prepare a Resilience Statement in the interest of good corporate governance and shareholder information.

Newly listed companies that fall within the remits of being mandated to produce this statement are likely to affect the public interest in the same way as other PIEs and should start as they intend to go on with respect to the proposed Resilience Statement.

22. Do you agree with the proposed minimum content for the Audit and Assurance Policy? Should any other matters be addressed in the Policy by all companies in scope?

We welcome the government agreeing with the Brydon Review to introduce a statutory requirement on PIEs to publish an annual Audit and Assurance Policy.

We also agree with the minimum criteria set out in the consultation.

23. Should the Audit and Assurance Policy be published annually and subject to an annual advisory shareholder vote, or should it be published and voted on at least once every three years?

We agree with the Brydon Review conclusion that the Audit and Assurance Policy should be three year rolling and put to an annual advisory vote by shareholders for approval at the Annual General Meeting. We welcome the government agreeing with the Brydon review recommendations on this.

We believe that such policies should be published annually in line with the Brydon recommendations.

27. Do you agree with the Government's proposal not to introduce a new statutory requirement at this time for directors to publish an annual public interest statement?

We are disappointed the government has decided not to introduce a new statutory requirement to introduce a Public Interest Statement as recommended by Sir Donald Brydon in his review.

We believe such a statement being a mandatory requirement by statute would provide an opportunity for directors to articulate in a holistic way how the company they govern serves the wider public interest and give an explanation by the directors of how they perceive the public interest in their company, and how they have taken measures to serve that interest over the previous year.

This statement could help to inform shareholders decisions in respect of where they invest and the scrutiny they provide.

Directors of PIEs have a responsibility that is arguably broader than just their own organisation given the impact PIEs can have in terms of the services they provide to the public and wider society. A statutory annual public interest statement setting out how directors of PIEs see how their entity serves the wider public interest would help keep them true to this and help both shareholders, employees and wider stakeholders understand how the directors of an entity view public interest in respect to how they govern their company.

Sir Donald Brydon also envisaged that there be three new reports by directors to improve director reporting to shareholders and other stakeholders: Audit and Assurance Policy, Resilience Statement, and a Public Interest Statement. It does not make sense that the government will press ahead with two of these on a statutory footing, but not the Public Interest Statement as well.

We envisage all three of Sir Donald Brydon's proposals for new reports by director of entities working alongside one another and think that without a statutory basis for all, the picture provided to investors and other stakeholders will be incomplete.

We urge the government to rethink introducing a statutory requirement for a Public Interest Statement by directors of PIEs.

31. Are there any existing or proposed directors' duties relating to corporate reporting and audit that you think should be specifically included or excluded from further elaboration for the purposes of the directors' enforcement regime?

We agree with Sir Donald Brydon that more details on what 'adequate accounting records' means should be undertaken. Sir Donald Brydon proposes this should be done as part of a review of the Companies Act and this White Paper seems to propose to give the new regulator, ARGA, the power to impose more detailed requirements as to how certain statutory duties relating to corporate reporting and audit are to be met by directors. When taking this forward the government should ensure there is no confusion on 'adequate accounting records' and that the Companies Act and the regulator say the same thing on this.

The Brydon Review also recommended that there 'should be an obligation for auditors to assess that the directors have maintained accounting records to a standard beyond the minimum level necessary for an audit to be performed.' We do not understand why the auditor would need to determine whether the accounting records maintained "to a standard beyond the minimum level necessary for the audit to be performed" – if they meet the minimum for audit, then they would be adequate for the auditor's purposes and questionable as to why the auditor would be asked to determine whether they go beyond that assessment.

32. Should directors of public interest entities be required to meet certain behavioural standards when carrying out their statutory duties relating to corporate reporting and audits? Should those standards be set by the regulator? What standards should directors have to meet in this context?

We agree that directors of PIEs should have to meet certain behavioural standards in the same way as their auditors.

It would seem appropriate that those standards are set by the regulator. Some directors of PIEs who are members of professional bodies including accounting bodies will already have to comply with a code of ethics enforced by the body to which they belong. It seems appropriate that directors of PIEs should all face a similar behavioural standard whether they are a member of a professional body or not.

As a minimum, directors should comply with the same standards of professional behaviour, integrity, competence to undertake and understanding of their fiduciary responsibilities, duty to declare and/or avoid conflicts of interest, and recognition of the public interest in their work that one would expect of professionally qualified directors.

35. Do you agree that a new statutory requirement on auditors to consider wider information, amplified by detailed standards set out and enforced by the regulator, would help deliver the Government's aims to see audit become more trusted, more informative and hence more valuable to the UK?

We agree that wider information should be considered, and this can be on a range of information from cyber security to sustainability, but what should be clear is what wider information an auditor is taking under scope in their audit, how this would differ from what the auditor considers today under the auditing standards, and whether this is part of the audit of the financial statements or something else.

Auditors are currently required to assess risk in planning and performing the audit, and in doing so inquires, observation, inspection and analytical procedures are undertaken. If the consideration of wider information is open ended it could in fact detract from audit quality, as auditors would not be able to focus on what they have (in their expertise) determined to be of most significance, but would rather be distracted by other areas that might not be relevant or out of scope of the audit of the financial statements. This could also lead to a greater expectation gap.

In regard to auditors considering director conduct, the IAASB's International Standards on Auditing (which are developed with input from the UK), include the consideration of the control environment

of an entity when performing an audit. The control environment includes governance functions and the attitudes, awareness, and actions of those charged with governance.

The concept of requiring auditors to "consider relevant director conduct" is very vague and would be very difficult to operationalise beyond what is done today in terms of understanding the control environment of a company without a more specific framework. For example, how would "director conduct" be evaluated and measured?

If auditors are requested to evaluate and assess a company's internal control over financial reporting, consideration of the control environment would be included. In the US and in many countries around the world, the COSO Framework is used to evaluate and assess internal control. The COSO Framework includes 17 principles that companies should have in place to achieve effective internal control. The principles with respect to the control environment includes considerations related to the organisation's commitment to integrity and ethical values among other important matters.

If something beyond what is in COSO Framework's control environment principles is contemplated by the proposal in 6.1.10, then specific direction regarding "relevant director conduct" and how it is to be measured and evaluated would be necessary

36. In addition to any new statutory requirement on auditors to consider wider information, should a new purpose of audit be adopted by the regulator, or otherwise? How would you expect this to work?

We do not agree with the purpose statement set out by Sir Donald Brydon and do not think the regulator should adopt it as it was drafted by Sir Donald Brydon.

The purpose statement proposed by Sir Donald Brydon says, 'Help establish and maintain deserved confidence in a company, in its directors…' The purpose of an audit is to facilitate confidence in the information produced by the company and its directors, including the financial statements. But an audit should not be viewed endorsing a company or its directors, something that in our view needs to be decided by users based on information in which they have confidence.

If the regulator adopts the purpose statement as has been drafted by Sir Donald Brydon, it could lead to a misplaced perception that an audit is providing complete confidence in an entity's continued viability. As we believe must be obvious, an audit is not forward looking, but can only base its conclusions on a snapshot of the current position.

Apart from this section of the proposed purpose of audit statement we agree with what Sir Donald Brydon proposed in relation to the purpose of audit statement. However, we agree that this shouldn't be written in law and mandatory. The new purpose of audit statement should be able to evolve, but with input of stakeholders including auditors, directors of entities and shareholders via the regulator.

37. Do you agree with the Government's approach of defining the wider auditing services which are subject to some oversight by the regulator via the Audit and Assurance Policy?

We agree that wider auditing services ought to be defined by the company's Audit and Assurance Policy. Every company may have different reasons, perspectives and needs in terms of wider auditing services. Allowing the definition of what is being sought in terms of wider auditing services to be within an entity's Audit and Assurance Policy will allow flexibility.

The illustration of the "new audit" model on page 97 is interesting. However, if the practitioner were to provide a reasonable level of assurance on the items identified that are outside of the financial statements (culture, ESG, cyber, controls, mineral reserves, other), the cost for an "audit" would increase dramatically.

40. Would establishing new, enforceable principles of corporate auditing help to improve audit quality and achieve the Government's aims for audit? Do you agree that the principles suggested by the Brydon Review would be a good basis for the regulator to start from?

The principles of corporate auditing set out by the review conducted by Sir Donald Brydon are very similar to what exists today under the professional standards. While those standards can always be improved upon, we do not think it is necessary to start from scratch. Rather, the existing principles and standards should be considered and evaluated. Any principles should be in line with an auditor's ethical responsibilities.

41. Do you agree that new principles for all corporate auditors should be set by the regulator and that other applicable standards or requirements should be subject to those principles? What alternatives, mitigations or downsides should the Government consider?

As per our answer to Question 40, we agree that the regulator should set the principles, but before any set of principles is agreed by the regulator, they should be subject to consultation. Any changes to the principles should be built upon those that exist under the professional standards and should be in line with an auditor's ethical responsibilities.

42. Do you agree with the Government's proposed response to the package of reforms relating to fraud recommended by the Brydon Review? Please explain why.

We agree that a holistic approach to fighting fraud is needed that involves directors, management, internal auditors, and external auditors.

We agree with the proposal to require directors of Public Interest Entities to report on the steps they have taken to prevent and detect material fraud. The duty and responsibility to detect and report on fraud does not solely rest with the auditor and directors of entities have and should take responsibility in this regard too.

This proposal will in law make the responsibility of a director in relation to the detection and prevention of fraud within their organisation unequivocal.

In relation to the Brydon recommendations to require auditors of Public Interest Entities, as part of their statutory audit, to report on the work they performed to conclude whether the proposed directors' statement regarding actions taken to prevent and detect material fraud is factually

accurate (and the related requirement that auditors be required to report on the steps they took to detect any material fraud and assess the effectiveness of relevant controls); we would generally endorse such transparency but question the extent of work necessary to report in this manner.

For instance, there is now guidance as to the meaning of "relevant controls"? The extent of work necessary for auditors to undertake these tasks needs to be more clearly explained by the regulator.

Requiring auditors to conclude whether the proposed director's statement regarding actions taken to prevent and detect fraud is factually accurate is beyond the reasonable level of assurance provided in an audit. This will have a cost implication for audits that needs to be fully understood.

We believe improving auditor education on fraud is important. We agree with the Brydon Review that fraud awareness and forensic accounting training form part of the qualification and continuous learning process for financial statement auditors. Continuing professional development is also important in this regard for all auditors (and the wider accounting profession too) and look forward to the FRC working with professional bodies in this regard.

We agree with the Brydon recommendation of a fraud register run by the regulator and look forward to ARGA pushing forward with this recommendation.

We also agree with the Brydon recommendation that ARGA establish an independent Auditor Fraud Panel to which it would refer the results of any investigations into auditor failure to detect material frauds and that such a Panel should be equipped with the ability to levy sanctions on auditors as appropriate. We invite the government to give this proposal closer consideration before dismissing it.

44. Do you agree that auditors' judgements regarding the appropriateness of any departure from the financial reporting framework proposed by the directors should be informed by the proposed Principles of Corporate Auditing? What impact might this have on how both directors and auditors assess whether financial statements give a true and fair view?

We agreed with the Brydon Review that the 'true and fair' wording in the Companies Act 2006 be replaced with "present fairly, in all material respects". This will bring the UK in line with other international wording on directors and auditors responsibility in relation to company accounts.

Given that a number of other jurisdictions use the wording 'present fairly, in all material respects' we do not recognise the government's claim that it carries the risk of unintended consequences, as there a number of international precedents the government might follow if it took this change on board.

We are pleased that the government and regulator accept the Brydon recommendation to create a new user guide to audit. We express the hope that the regulator does adopt the Plain English Campaign guidance in its drafting.

However, we do think that the new user guide should be created alongside a change to the 'true and fair' wording in the Companies Act 2006 being replaced with "present fairly, in all material respects".

We think failure to replace "true and fair" will still leave an expectation gap.

45. Do you agree that the need for specific assurance on APMs or KPIs, beyond the scope of the statutory audit, should be decided by companies and shareholders through the Audit and Assurance Policy process?

Yes. We agree that shareholders should decide whether there is a need for specific assurance on APMSs and KPIs beyond the scope of the statutory audit and that the appropriate vehicle for this is Audit and Assurance Policy process.

48. Do you agree that a new, distinct professional body for corporate auditors would help drive better audit? Please explain the reasons for your view.

We do not agree that a distinct professional body for corporate auditors would drive better audit. There is little evidence to suggest that the professional bodies in the UK who currently regulate auditors fail to provide training, ethics guidance and enforcement, continuing professional development or any other aspect of regulation to the necessary standard, whether their members are accountants or auditors.

Creating a new professional body for auditors will not be an easy task. It will consume considerable resources – which are ultimately likely to be funded by businesses - to get to the point where it is a competent and functioning body. We believe those resources could be better deployed by BEIS ensuring that the new proposed regulatory system for audit is functioning well. We believe that will do more to drive better quality audits than the creation of a new professional body solely for auditors.

The UK is a world leader in developing professionals. Its professional membership bodies, including the current accounting and auditing bodies, have a global market and an excellent reputation in delivering respected professional qualifications. We do not see that the introduction of a further professional body for corporate auditors will improve matters – instead it may serve to cause confusion and undermine the current standing of the professional bodies that currently regulate audit.

The proposals outlined in the White Paper are in part designed to drive greater competition in the audit market. We agree greater competition would be a positive thing. However, the proposal to create a new professional body just for corporate auditors would remove the element of choice of audit qualification available to the market, paradoxically reducing competition between the professional bodies.

Creating a single professional body for corporate auditors would remove competition in this space and we think over the longer-term this is likely to be detrimental to standards, professional development and invocation in the training, support and regulation of corporate auditors.

Another consequence of this approach could be to strip the existing professional bodies of experienced staff, as the new body looks to find the necessary expertise. It appears likely that such expertise will be derived mainly among those who work and operate within the existing professional body framework. It follows that there may be adverse consequences for the

oversight, support and continuing professional development of the rest of the ecosystem of accounting and audit, at least in the short-term.

We think a full cost benefit analysis of this proposal should be shared with stakeholders before the government commits on this this path.

49. What would be the best way of establishing a new professional body for corporate auditors that helps deliver the Government's objectives for audit? What transitional arrangements would be needed for the new professional body to be successful?

Please see answer to question 48. We do not agree with this proposal.

50. Should corporate auditors be required to be members of, and to obtain qualifications from, professional bodies that are focused only on auditing?

Please see answer to question 48. We do not agree with this proposal.

We think that auditors obtaining qualifications from professional bodies that are broader than just audit is a positive. This means they are likely to obtain cross skilling and expertise in more than one field which they can then employ and use in their audit.

Audit requires a mix of talents and understanding to be done effectively. We worry that by having a body purely focussed on audit some of these extra skills and expertise derived from membership of an accounting professional body will be lost and this has the potential to harm audit in the long-term.

These proposals could also make it harder for an accountant or other finance professional to retrain and go into audit and therefore resulting in the audit profession becoming less accessible as they would need to join a new professional body to do so and this creates another layer of bureaucracy .

This proposal could also reduce the pipeline of auditors and increase regulatory costs for firms that train them, and this may mean investment is moved away from less profitable auditors and towards more profitable accountants and consultants.

51. Do you agree that a new audit professional body should cover all corporate auditors, not just PIE auditors?

Please see answer to question 48. We do not agree with this proposal.

However, if the government proceeds with this proposal, we think that creating a new professional body will be challenging in itself and then requiring it to take on more auditors than just those conducting PIE audits will add further complication and need further resource to be effective.

If the government does decide to go this route of creating a professional body for corporate auditors, it should only apply to PIE auditors and more than one professional body should be created.

A better approach altogether would be that the existing professional bodies work with the regulator to create a separate credential in PIE audit. This could be similar to the GMC which has a specialist register for plastic surgeons. Once this special credential is created all professional bodies who are regulated by ARGA could deliver it to their members who are in the PIE audit practice and the regulator could assess their ability in delivering the credential.

Please see answer to question 48 for more details.

54. Do you agree with Sir John Kingman's proposal to give the regulator the power to appoint auditors in specific, limited circumstances (i.e. when quality issues have been identified around the company's audit; when a company has parted with its auditor outside the normal rotation cycle; and when there has been a meaningful shareholder vote against an auditor appointment)?

We have concerns around the regulator having the power to appoint auditors in specific, limited circumstances. If an auditor has parted with the company it is auditing outside its normal rotation period or there has been a meaningful shareholder vote against an auditor appointment these are decisions and actions that are very unlikely to have taken place without good reason.

If a Public Interest Entity cannot obtain a new auditor this must signal serious concerns with that business and its management.

An auditor should not be appointed to take on an audit of such a PIE if it has not freely agreed to take on and tender for this work. An important part of the capitalist market system in which the UK operates its business within is the ability for businesses not to be forced to take on work and clients they do not wish to do business with.

We believe in these limited circumstances the judgement of the market and consumers is likely to provide a better solution to the perceived problem.

55. To work in practice, ARGA's power to appoint an auditor may need to be accompanied by a further power to require an auditor to take on an audit. What do you think the impact of this would be?

We do not agree with ARGA having such a power as we have answered in Question 54. An audit firm should be able to freely choose whether they audit a company or not and should not have an audit engagement they do not wish to take on forced upon them.

We also have concerns that if ARGA had this power, they may inadvertently be inclined to prefer availability over suitability for appointing an auditor to the potential detriment of the investor community.

56. What processes should be put in place to ensure that ARGA can continue to undertake its normal regulatory oversight of an audit firm, when ARGA has appointed the auditor?

Please see answer to question 54 and 55.

57. What other regulatory tools might be useful when a company has failed to find an auditor or in the circumstances described by Sir John Kingman (i.e. when quality issues have been identified around the company's audit; when a company has parted with its auditor outside the normal rotation cycle; and when there has been a meaningful shareholder vote against an auditor appointment)?

Please see answers to questions 54, 55 and 56.

58. Do you agree with the proposals and implementation method for giving shareholders a formal opportunity to engage with risk and audit planning? Are there further practical issues connected with the implementation of these proposals which should be considered?

Shareholders are the primary users of company accounts and we broadly support moves to increase shareholder understanding of the audit process, so audit and wider company reports, and accounts remain relevant and useful to them.

However, we think some the proposals outlined by the Brydon Review and accepted by the government in this White Paper need some further thought and consideration.

We have concerns with Sir Donald Brydon's original proposal that the audit committee should publish a formal invitation to shareholders to express any requests they have regarding the areas of emphasis they wish the auditor to incorporate in the audit plan. We think that the government is right to say that a shareholder views via such a mechanism is advisory in nature.

This proposal still does leave a number of questions unanswered: would shareholders then be limited to commenting on risks identified by the directors; could shareholders raise their own risks, no matter how uninformed; would auditors be committed to responding to risks raised by shareholders; would the economics of the audit be impacted by risks raised?

We recognise the government have said that the auditor would not be required to consider proposals which fall outside of the scope of the company audit, but there is potential for that to take place. We have some concerns that such a process may drive up the cost of an audit and be ineffective.

If shareholders are going to have access to the latest risk assessment we believe it is right that the audit committee should have the authority to make further disclosures to shareholders and limited to where there has been a material change to the principal risks facing the company since those previously disclosed in the last annual or interim report.

The obligation on auditors to consider suggestions put forward by shareholders and to provide feedback to the audit committee on the extent to which these have been adopted could be open ended with the auditor responding to anything raised by shareholders defacto. We agree that if this recommendation is taken forward it should be managed via the audit committee and auditors should only be expected to respond where the suggestions are relevant to the scope of the audit and assurance the auditor is providing for that entity.

Investors must have confidence in the audit process, but this does not mean they should be allowed to dictate the terms of an audit or the areas of risk identified in the audit process. This should be the role of the auditor with oversight by the audit committee and the directors of an

entity. The audit committee should be engaging with shareholders to seek their input and we are pleased to see that is the way the government are heading in these proposals. However, many questions remain around the proposals for shareholder involvement and we think before these are implemented a further consultation with more details set forward by ARGA is needed.

These proposals also have a huge potential to increase the cost of an audit and may not provide much further benefit to investors.

59. Do you agree with the proposed approach for ensuring greater audit committee chair and auditor participation at the AGM? How could this be improved?

We were not opposed to there being a standing agenda item at AGMs on questions to the audit committee and auditor as proposed in the Brydon Review. But if an auditor was to attend, they should only be expected to answer questions that related to their audit and not beyond.

We do not think asking the regulator to update their guidance and work within the existing framework is going to be enough to change much in terms of shareholder engagement in the process.

As we mentioned above in answer to Question 58 the problem seems to be between communication and engagement between the audit committee and shareholders. To improve this link the government should have made it a mandatory standing agenda item for PIEs that the audit committee chair attends, provides a report to shareholders and takes questions from them.

We think this would improve the engagement between the audit committee and shareholders and mean that the audit committee has a greater awareness of shareholder views when they seek a new auditor and what shareholders would like assurance on.

60. Do you believe that the existing Companies Act provisions covering the departure of an auditor from a PIE ensure adequate information is provided to shareholders about an auditor's departure? If you believe those provisions are inadequate, do you think that the Brydon Review recommendations will address concerns in this area? What else could be done to keep shareholders informed?

Arguably the Companies Act already carries legal provisions for shareholders to call a meeting when an auditor has suddenly resigned or been dismissed. The regulator could do more to encourage the use of the already existing powers.

We believe a more clearly defined statement by the auditor which lists out the reasons for them resigning would be an appropriate way to inform shareholders as to reasons why they are leaving. We agree with point 7.3.14 on page 134 of the White Paper.

We do not agree it would be appropriate for an auditor who departs from auditing a PIE to have to answer questions by the shareholders. This would invite a number of legal issues. If auditors were required to answer questions by shareholders, it could become a quasi-legal proceeding with attorneys for all parties present and likely lead to limited (or no) answers anyway.

Before the government presses ahead with reform in this area it should carefully consider the litigation issues any of the proposed changes could create and ensure appropriate mitigation is in place.

We do not support the proposal that the regulator should have the power to appoint auditors in specific, limited circumstances. We do not think it is appropriate or in the public interest to force an auditor to perform an audit. In answer to other questions in this consultation we have gone into greater detail as to why this is our view.

61. Should the 'meaningful proportion' envisaged to be carried out by a Challenger be based on legal subsidiaries? How should the proportion be measured and what minimum percentage should be chosen under managed shared audit to encourage the most effective participation of Challenger firms and best increase choice?

We do not support and have concerns about the proposed managed shared audit the government has outlined in the White Paper. While we are pleased the government is not adopting the CMA's proposals for joint audit, we believe that what the government is putting forward will still face many of the same challenges and difficulties that the CMA proposal faced.

These challenges and issues include:

- Does not address that fact that many PIEs are multi-national and therefore require multi-national auditors. Many 'challenger' firms will not have that international reach to be able to support managed shared audits.
- Could result in disincentivising innovation.
- Still doesn't address the lack of 'challenger' firms in the UK audit market able to engage even at the level proposed in the audit of a PIE.
- Will raise audit costs for little benefit to the entity being audited.
- Unlikely to increase competition.
- Doesn't address that some 'challenger' firms will still have a lack of capacity or experience to be able to even engage in the managed shared audit process.

We do not believe the government has addressed these challenges in this White Paper.

This proposal could have the adverse effect of PIEs refusing to appoint a 'challenger' firm as their sole auditor because of the perception that 'challenger' firms only have the capacity, knowledge, experience and expertise to be able to audit subsidiaries, meaning that the PIE will always require one of the Big 4 to conduct audits alongside them for a successful audit of the whole entity.

This approach also relies on the bigger 'challenger' firms below the Big 4 wanting to engage and be part of managed shared audits. If recent media reports are reliable it suggests some of the bigger 'challenger' do not wish to participate in this process.[2] If that is the case it could make this proposal much harder to implement, then it already is.

This proposal could also create the adverse effect where not only do you have a Big 4, but than a 'smaller 4' below that engage in managed shared audit and no other firms that take part in the process. Instead of enhancing competition and resilience in the market it could do the complete opposite.

[2] UK plan to shake up audit market faces major setback | Financial Times (ft.com)

62. How could managed shared audit be designed to incentivise Challenger firms to invest in building their capability and capacity? What, if any, other measures, would be needed?

The White Paper does not identify many ways it can help 'challenger' firms build their capability and capacity to engage successfully in the proposed managed shared audit proposal. In answer to Question 61 we outline our concerns with this proposal and why we do not think it will work.
We think measures proposed earlier in the White Paper to increase the number of PIEs will do more to get 'challenger' firms doing audits than managed shared audit will. This is because new PIEs will be more used to using audit firms outside the Big 4 and likely to continue to do so. Once FTSE 350 companies see that audit firms outside of the Big 4 conduct good quality audits of entire PIE entities, it is more likely they will consider them when their audit comes up for tender.

63. Do you have comments on the possible introduction in future of a managed market share cap, including on the outlined approach and principles? Are there other mechanisms that you think should be considered for introduction at a future date?

We are not in favour of the introduction of a managed market shared cap and do not agree with the government's recommendations in this space.

Under this proposal the regulator could limit the choice of PIE in who they could appoint as an auditor to just 'challenger' firms. Entities should be allowed to choose the auditor which is right for their organisation. Under these proposals instead of enhancing choice the government is taking it away and we do not believe that this will drive better quality audits.

The proposals do not say how the regulator will take account of a 'challenger' firm capabilities and experiences to conduct the audit for which they are putting them forward. More details need to be given on this before this proposal is taken forward.

The proposed market share cap could also harm audit quality, as PIEs are limited to who they can appoint as an auditor, and the regulator may not necessarily choose a cohort of 'challenger' firms who are right for that entity.

The market share cap presumes that the 'challenger' firms would want to take on the whole group audit, but there may be circumstances where this does not happen. The White Paper has not given thought to this possible circumstance.

This proposal could also harm investor confidence as shareholders who have invested in a PIE that is forced to take on a 'challenger' firm for their forthcoming audits may think and believe that the audit firm doesn't have the experience and capabilities to perform the audit adequately. This could lead to a lack of trust in the assurance being received and therefore a lack of appetite for shareholders to invest or keep their shares.

64. Do you have any further comments on how the operational separation proposals should be designed, codified (in legislation and regulatory rules), and enforced in order to achieve the intended outcome of incentivising higher audit quality?

We note that the Big 4 firms in the UK are already working with the FRC on voluntary proposals in line with what the CMA and the government have proposed about operational split between their audit and advisory arms.

We still have concerns around the operational split proposals and do not think they will deliver the desired outcomes.

We still think the proposals for operational splitting of the Big 4 audit firms will lead to:

- Less cross-skilling of auditors
- Less investment in technology from the Big 4 for audit purposes
- Increased audit costs
- Potentially a reduction in the quality of audit as firms find it more difficult to attract talent away from the advisory side of their firm and less ability to hire specialists
- Limiting career opportunities for auditors and making audit a less attractive career prospect
- In the longer-term could lead to some audit firms focussing solely on advisory side and not taking on PIE audits anymore

The proposals still don't address the international challenge - given the international nature of the large audit firms, it may prove challenging to have firms being restricted in service provision in one jurisdiction but not in another.

We believe a multidisciplinary model is an important contributor to high quality audits. The separation of audit and non-audit practices puts that model in jeopardy. The White Paper includes a statement that "the multidisciplinary structure within large firms has resulted in behavioural and financial incentives that undermine both attributes and sometimes lead to poor audits." This is a convenient argument when there is an audit failure when, in reality, the opposite is true – that a multidisciplinary model leads to high quality audits – because the auditor has the ability to draw upon expertise within their firm to assist with complex specialised areas of the audit.

We welcome the government including in this consultation a definition of when audit firms will be required to operationally split from their advisory side, this was missing from previous consultations on this issue. The White Paper states 'The Government envisages that the measures described below will apply initially to audit firms who carry out statutory audits of 15% or more of the FTSE 350 by audit fees…. it will ultimately be for the new regulator to determine the initial scope of these measures and then adjust it over time to reflect future changes to the structure of the market.'

We think this proposal could mean 'challenger' firms could be disincentivised from taking up more audits of FTSE 350 firms and operate just below the proposed 15% of FTSE 350 audit fees level in order to maintain their multi-disciplinary model.

If they do breach this 15% limit or whatever limit is introduced in future it could also present challenges for a 'challenger' firms ability to continue to conduct audits in the PIE space, as they

will still likely be relying on the capacity, expertise, technology, specialisms and knowledge from their non-audit side of their firm to help conduct PIE audits.

Finally, there is no evidence that audits performed by the largest firms are of a lower quality than those provided by 'challenger' firms. We do not believe there is evidence that shows that audit quality is diminished by multi-disciplinary firms. There have been issues with audit of PIEs by both the Big 4 and 'challenger' firms in the recent past, but also examples of good quality audits by both. The evidence does not point towards poorer quality audits because of the multi-disciplinary audit firms.

66. In the event that the Government wishes to go further than the existing operational split proposals in future and implement split profit pools in line with the CMA recommendation, do you have any comments on how these can be made to work effectively?

We do not agree with the proposals to operational split audit firms and have provided answers to this question in answer to Question 64.

67. The Government believes these proposals will meet its objectives. In the event that they prove insufficient to improve audit quality, and full separation of professional services firms is required, do you have any comments on how to make this work most effectively?

We do not agree with the proposals to operational split audit firms and have provided answers to this question in answer to Question 64.

68. Do you have comments on the proposed measures? Are there any other measures the Government should consider taking forward to address the lack of resilience in the audit market?

We were supportive and agreed with CMA partner clawback measures they proposed in their Statutory Audit Market Study.

We welcome that the government has chosen not to focus on CMA ownership rules proposals at this time. If they are to be reconsidered, we would be concerned about ownership rules for a firm being loosened to permit majority ownership and control by non-auditors as the business incentives might shift unintentionally to being less focused on quality. While acknowledging that changing ownership rules may encourage greater capital investment and foster positive innovation, with that investment we might expect a greater emphasis on returns to those investors, especially non-auditor investors, without an appropriate quality balance. This may also result in the profession no longer being viewed as a profession but more as a business enterprise.

72. Do you agree with the Government's approach to component audit work done outside the UK? How could it be improved?

Some jurisdictions have laws that would prevent a UK group auditor from providing a UK regulator with access to overseas component working papers. To solve this issue the UK regulator needs to work with its counterparts to reach agreement on how to handle. Firms should not be put in the position of having to meet one regulator's demands, while violating another regulator's or government's rules.

73. Do you agree that it is problematic if documents that the auditor reviewed as part of the audit are unavailable to the regulator because of the audited entity's legal professional privilege? If so, what could be done to solve or mitigate this issue while respecting the overall principle of legal professional privilege?

We agree that it may be problematic if documents reviewed as part of the audit are unavailable as a result of legal professional privilege, not only because such documents may inhibit the regulator's ability to investigate the case, but also because it may prejudice those under investigation if they (or their client) hold privileged documents which might help their defence as they will be unable to produce that material to their regulator (even on a confidential basis) without the consent of the privilege holder.

The obvious way to deal with this would be to enshrine in law the situation identified by Lord Hoffman in R (Morgan Grenfell & Co Ltd) v Special Commissioner of Income Tax [2002] UKHL 21 (i.e. that where a regulator has a statutory power to request documents, there is no infringement of the legal professional privilege when documents are handed over in response to a request made under that power), subject to the qualifications identified in the Sports Direct case – and accepted by the FRC in that case – namely: (i) the request for the information must come from a regulator; (ii) the regulator must be bound by duties of confidentiality in its use of the information; and (iii) the holder of the privilege must be someone other than the person who is at risk of some adverse finding as a result of the use of the information by the regulator.

74. Do you agree with the proposed general objective for ARGA?

While the proposed general objective: "to protect and promote the interests of investors, other users of corporate reporting and the wider public interest", is certainly more broadly framed than the objective proposed by the FRC Review, we feel that it may encourage some confusion about ARGA's remit (suggesting as it does a primarily consumer focus) and seems unhelpfully to de-emphasise the importance of ensuring adequate standards in audit, corporate reporting and corporate governance identified by the Review by creating a separate "Quality objective". We have long argued that a key aim for ARGA, and a major step in ensuring boardroom hygiene, must be to regulate the entire boardroom, rather than only those directors who happen to be professionally qualified. The general objective seems to be directed somewhere else. We also believe it would be better that this objective (rather than the proposed Quality objective) retain the explicit mention of ARGA's remit to set (rather than merely "promote") high standards of statutory audit, corporate reporting, and corporate governance.

75. Do you agree that ARGA should have regard to these regulatory principles when carrying out its policy-making functions? Are there any other regulatory principles which should be included?

Promoting innovation in statutory audit work, corporate reporting and corporate governance. Promoting brevity, clarity and usefulness in corporate reporting. Working closely with other regulators from the UK and internationally. Anticipating emerging corporate governance, reporting or audit risks by being forward-looking and acting proactively where possible.

The proposed regulatory principles seem to be more a collection of strategic aims than principles which describe how ARGA will seek to set policy. While we appreciate that ARGA will also adopt the Regulators' Code, it seems to us that the regulatory principles should include a commitment only to promote policy that is rooted in evidence and which is proportionate to the end sought. We also have a concern that "promoting innovation" may become an excuse for the consequences of ill-thought out or reckless corporate governance, which may be incompatible with ARGA's role as regulator.

76. Should the scope of the regulator's oversight arrangements be initially confined to the chartered bodies and should they be required to comply with the arrangements?

While we welcome the move to formalise the oversight arrangements with ARGA via a memorandum of understanding, which will permit clarity as to expectations, we do not see the evidence that justifies requiring the chartered bodies to comply with oversight via legislation. All the chartered bodies have worked effectively with the FRC under existing arrangements and we are not aware of any incident or case reported by the FRC that would suggest that the chartered bodies have shirked their responsibilities or have otherwise created a regulatory risk that might have required action.

The risk, in our view, is that imposing a further and expensive layer of regulation on the chartered bodies, funded by them and their members, will in fact disincentivise membership, with all the benefits that proper qualifications and professional regulation offers in the public interest. In particular, many of our members are likely to be CFOs or other C-Suite employees. Imposing the burden of regulation solely on those who are members of the chartered bodies seems calculated to encourage them to cease membership, which is unlikely to encourage the objective of improved corporate governance.

While the consultation suggests that regulating accountants who are either unregulated or who do not belong to a professional accounting body is likely to be disproportionate, we respectfully suggest that in areas of risk such as money laundering, the problem is likely to be more prevalent amongst that population that amongst chartered accountants who volunteer for regulation and AML supervision. This is not only unfair, but equally is against the public interest in ensuring all those who purport to be fit to provide accounting and financial services are adequately trained and supervised.

77. What safeguards, if any, might be needed to ensure the power to compel compliance is used appropriately by the regulator?

While our primary position is that the existing voluntary arrangements have worked well (and therefore there is no evidence that such a power is needed), we agree that if that power is granted to ARGA it should be limited to CIMA's regulatory functions, and even then to the minimum degree necessary to ensure compliance. We apprehend that there is a risk of creating a significant bureaucracy to second guess operational decisions which have little impact on outcomes or the public interest. Accordingly, the power to compel compliance should only be exercised where there is evidence of serious misconduct or incompetence in the handling of its regulatory functions or there is a serious risk that public confidence in the accounting professions may be undermined.

Although the consultation recognises the risk of overlap with other regulatory agencies, e.g. OPBAS or OFQUAL, it nonetheless identifies training and qualifications (which would be within OFQUAL's remit so far as Apprenticeships are concerned) and licensing and practice assurance (which is very much concerned with AML supervision, under the scrutiny of OPBAS) as areas of focus. This demonstrates the risk of regulatory overlap and the potential for unnecessary regulatory costs for the chartered bodies and their members.

78. Should the regulator's enforcement powers initially be restricted to members of the professional accountancy bodies? Should the Government have the flexibility to extend the scope of these powers to other accountants, if evidence of an enforcement gap emerges in the future? What are your views on the suggested mechanisms for extending the scope of the enforcement powers to other accountants (if it is appropriate at a later stage?

While we welcome the proposed extension of the new regulators' powers to company directors, in a market where we compete with a number of bodies that are either unregulated or subject to significantly lighter regulation, we suggest that these measures can only lessen the incentives to becomes members of a chartered body. Indeed, research among our members tends to suggest that as members progress towards board level, their CIMA qualification and title becomes increasingly less relevant than their work experience.

Given that the package of measures outlined will undoubtedly increase the costs of membership and expose members to a greater risk of professional sanction (despite the intention to include the entire boardroom within ARGA's scope), we think there is a significant risk that making only chartered accountants subject to the enforcement powers is likely to encourage a drift away from the chartered bodies, undermine one the intention to increase standards of corporate reporting and corporate governance and distort the market in favour of the non-chartered accounting bodies. It seems unhelpful for the consultation to suggest that action to remedy the enforcement gap may only occur after the professional accounting bodies have suffered a significant decline in membership, as we suggest that it is not likely to encourage increased standards in the market for any of the chartered bodies to go out of business.

It is not clear what evidence is relied upon to suggest that it would not be proportionate to extend regulation to non-member accountants (and or the avoidance of doubt, it would be helpful to see that evidence or any associated risk assessment). In our view, the government should not only have the flexibility to extend regulation to the non-regulated but should in fact do so.

As regards the mechanism to deal with any enforcement gap, we agree that as a general principle, all regulation should be targeted and proportionate. We are however unsure of the logic that would only require the unqualified to be regulated when providing accounting services to public interest entities but remain free to do so to anyone else, without better explanation of the scenarios envisaged.

79. Should the regulator be able to set and enforce a code of ethics which will apply to members of the chartered bodies in the course of professional activities? Should the regulator only be able to take action where a breach gives rise to issues affecting the public interest? What sanctions do you think should be available to the regulator?

In our view, for ARGA assume the role of setting and enforcing the code of ethics for members of the chartered bodies would significantly compromise their autonomy. The ability (in the words of CIMA's Royal Charter): "…to frame and establish rules (by way of Bye-law, regulation, code, or guidelines of any kind) for observance in all matters pertaining to professional practice therein…" is a key responsibility and one that is closely associated with CIMA's function in educating management accountants, setting appropriate examinations (including in the area of ethics) and operating its own professional conduct procedures, all of which feeds into the development of a code of ethics titrated to the needs of management accounting. Although this suggestion seems to envisage the chartered bodies contributing to "their" code is some way, this would be a significant intervention in the operations of the chartered bodies and does not sit comfortably with the role of oversight regulator.

We agree that ARGA should be able to take action wherever a public interest issue arises and not just where the work involves a public interest entity. Our experience is that we have referred public interest cases to the FRC in recent years, for instance one involving an NHS body criticised by the Audit Commission, where despite the clear public interest aspects to the case, the FRC felt it did not meet the test under the Accountancy Scheme, We believe that public confidence in the accounting professions will be better served by a somewhat wider scope for action.

We take the view that the sanctions currently available to the FRC remain appropriate and there is no compelling case to change these.

94. Are there others matters which PIE auditors should have to report to the regulator? Could this duty otherwise be improved to ensure that viability and other serious concerns are disclosed to the regulator in a timely way?

In response to the Independent Review of the FRC we said that while we broadly supported Recommendation 50: 'In the most serious cases, the Review suggests it may be appropriate for the regulator to issue a report to shareholders suggesting that the company's dividend policy should be reviewed, or that they consider the case for a change of CEO, CFO, chair, or audit committee chair, or for other strengthening of the board of directors. The Review believes that, where the severity of the facts merits it, the regulator should have the confidence to do this. Decision-making should rest, as now, with boards and shareholders' it would be useful to expand on what issues of 'serious concern' look like. This remains the case now and we would like to see the regulator do further work to identify issues they see may qualify as 'serious concerns' and consult on these findings.

In our response to the Independent Review of the FRC we also said that decision making should still rest with boards and shareholders and we maintain that view even when issues of serious concern have been raised.