

## Strategy 2018/21

### Draft budget and levy proposals 2018/19

A public consultation issued by the Financial Reporting Council (FRC)

Comments from ACCA  
February 2018  
Ref: TECH-CDR-1688

ACCA (the Association of Chartered Certified Accountants) is the global body for professional accountants. We aim to offer business-relevant, first-choice qualifications to people of application, ability and ambition around the world who seek a rewarding career in accountancy, finance and management.

Founded in 1904, ACCA has consistently held unique core values: opportunity, diversity, innovation, integrity and accountability. We believe that accountants bring value to economies in all stages of development. We aim to develop capacity in the profession and encourage the adoption of consistent global standards. Our values are aligned to the needs of employers in all sectors and we ensure that, through our qualifications, we prepare accountants for business. We work to open up the profession to people of all backgrounds and remove artificial barriers to entry, ensuring that our qualifications and their delivery meet the diverse needs of trainee professionals and their employers.

We support our 200,000 members and 486,000 students in 180 countries, helping them to develop successful careers in accounting and business, with the skills required by employers. We work through a network of 101 offices and centres and more than 7,200 Approved Employers worldwide, who provide high standards of employee learning and development. Through our public interest remit, we promote appropriate regulation of accounting, and conduct relevant research to ensure accountancy continues to grow in reputation and influence.

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## GENERAL COMMENTS

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ACCA welcomes the opportunity to comment on the FRC's proposed strategy for 2018/21 and its draft budget and levy proposals for 2018/19.

We are pleased to see that integrity in business features highly in the FRC's mission, with appropriate references to corporate culture and values, and the importance of businesses being seen to 'do the right thing'. In fact, the word 'integrity' is mentioned 11 times throughout the consultation document, including 5 times in relation to the FRC's mission and 3 times in relation to the FRC's *own* transparency and integrity (on page 2). It is disappointing to see that the only meaningful reference to integrity *in business* is in the subheading on page 3. However, that section focuses on the damage done to public confidence in business as a result of *past* corporate governance scandals and audit failures. It states that the FRC should do more to identify new and emerging challenges and risks, but there is no focus on how corporate culture and values may be influenced, in order to promote integrity in business.

Naturally, the consultation document makes several references to the UK's exit from the EU. At this stage, the impact of Brexit remains very uncertain, and so the document sets out only continuing activities.<sup>1</sup> However, it also refers to challenges to be faced, 'including new tasks resulting from the UK exit from the EU'.<sup>2</sup> At this stage, it is unclear whether there will be any such new tasks.

## AREAS FOR SPECIFIC COMMENT

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In this section, we set out our responses to the specific questions raised throughout the consultation document.

### **Question 1: Do you have any comments on our strategic priorities - are they in line with your expectations or are there other issues on which the FRC should focus?**

Section Two considers the FRC's strategic priorities under five distinct sub-headings. Some of these are discussed in detail below. However, none of the five sub-headings relates to the FRC's independent survey of views on the FRC's effectiveness, referred to in Section One. We note the statement, arising out of the survey, that 'Overall, the FRC is considered independent of the professions it regulates, although investors expressed some concerns about the role of former auditors within the organisation.'<sup>3</sup> We note the introduction of a register of interests for Board and committee members. However, in light of the current discussions about the perceived independence of international standard-setters, we would expect the concern over 'the role of former auditors within the organisation' to be addressed in the final strategy for 2018/21.

We note also the following statement:

*'We are independent from those we regulate, with a strong public interest ethos. But we also need the technical skills, practical experience and the authority to set, influence and monitor codes and standards. This requires our people to be experts in their field with industry experience, so as to have the authority to set and influence national and international*

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<sup>1</sup> Under the sub-heading 'UK Exit from the EU', the consultation document only refers to *continuing* to work closely with international organisations, and to deliver its responsibilities as UK competent authority for audit.

<sup>2</sup> Strategy 2018/21 and Draft Budget and Levy Proposals 2018/19, page 4

<sup>3</sup> Strategy 2018/21 and Draft Budget and Levy Proposals 2018/19, page 2

*standards.*<sup>4</sup>

This paragraph is likely to be perceived as an assertion that the status quo is satisfactory. We suggest that it should be amended to express an intention to address the challenge of balancing the need for independence with the need for experience.

#### *Promoting corporate governance and investor stewardship with a long term focus*

We welcome the FRC consultation on a revised UK Corporate Governance Code. ACCA will be responding to the FRC's proposals. It is essential that this work addresses issues of public trust in business and, as stated, 'aims to ensure the attractiveness of the UK capital market to global investors', during the current period of uncertainty.<sup>5</sup>

We are equally interested in the FRC's follow-up activities to assess the effectiveness of the Code, including monitoring 'the way in which companies have reported meaningfully on how they have applied [the Code's] principles'.<sup>6</sup> We also look forward to engaging with the FRC when it later consults on the future direction of the UK Stewardship Code.

#### *Promoting true and fair reporting*

We welcome the range of activities identified in this section of the consultation document, and the commitment to respond to developments in wider reporting. We agree that investors value comparability of information, and UK alignment to international accounting standards is crucial to maintaining standards and providing that much-needed comparability. Nevertheless, the FRC must remain mindful of the need to balance demand for high standards of corporate reporting with the aim of reducing the regulatory burden on business. The passing mention of IFRS endorsement post-Brexit in the consultation document is reasonable, given the current level of uncertainty.<sup>7</sup>

IFRS 17, *Insurance Contracts* is mentioned in the consultation document in the context of assessing progress on the strategic priority of promoting true and fair reporting. This standard is unlikely to have been endorsed before March 2019, and therefore it is likely to be subject to any new endorsement regime. The FRC must also consider, at an early stage, how it will amend UK GAAP for insurance companies, as there are many unlisted insurance companies and subsidiaries of listed groups. IFRS 17 will involve systems changes, and running a number of different systems is likely to be problematic.

The consultation document, in fact, makes no mention of the FRC's role in relation to UK GAAP, which we find surprising. ACCA believes that UK GAAP should maintain its alignment to the main accounting principles and treatments of IFRS. In assessing progress against the strategy to 2021, we would have expected to see reference to an assessment of the impact of the new standards (IFRS 9, 15 and 16), which will be implemented by listed companies in the period 2018 to 2019, with a view to the application to unlisted companies via FRS 102. (FRS 101 will also require updating on a regular basis.)

At some point in the period covered by the proposed strategy, there should be a review of the impact of the new UK GAAP introduced in 2015/16. ACCA would like to see a focus on the consequential loss of information on the public record in respect of small and micro companies.

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<sup>4</sup> Strategy 2018/21 and Draft Budget and Levy Proposals 2018/19, page 20

<sup>5</sup> Strategy 2018/21 and Draft Budget and Levy Proposals 2018/19, page 7

<sup>6</sup> Strategy 2018/21 and Draft Budget and Levy Proposals 2018/19, page 8

<sup>7</sup> Strategy 2018/21 and Draft Budget and Levy Proposals 2018/19, page 10

### *Promoting high quality audit and assurance*

We support the steps taken so far by the FRC to monitor audit quality, which are essential if audit quality is to continue to improve. The consultation document states that progress towards the aim of at least 90% of FTSE 350 audits requiring no more than limited improvements will be assessed in the FRC's 2019 annual report on Developments in Audit. It goes on to state that the FRC will 'consider increasing the target percentage and broaden its application'. It is not clear in what way it will be broadened.

We should like to draw the attention of the FRC (and other stakeholders) to ACCA's publication *Tenets of a quality audit*, which sets out some of the tensions inherent in determining what constitutes quality. The report is available at <http://www.accaglobal.com/uk/en/professional-insights/global-profession/Tenets-of-quality-audit.html>. We would also urge the FRC to engage with this report when carrying out work to consider what 'the audit of the future' might look like. The consultation document expresses a bold intention to test the current statutory audit model. While we are supportive of potential change, we anticipate that significant challenges will be encountered, and we would encourage a collaborative approach. ACCA would be very keen to be part of 'a broad and diverse coalition' to address the aims and challenges.<sup>8</sup>

With regard to standard-setting, ACCA believes that auditing standards should be aligned to ISAs, as far as possible. We believe that the FRC should commit to implementing ISAs in their entirety, except in cases where to do so would be impossible according to UK law, or where there are significant policy reasons to go further.

### *Effective enforcement*

The consultation document explains that recently-acquired powers to obtain information and documents from some entities, together with the possibility of a greater range of conduct attracting a sanction, has led to a further strengthening of the FRC's team. However, the direct impact of these changes on the relevant staff costs has not been quantified.

### **Question 2: Do you have any comments on our proposed audit firm monitoring approach?**

We welcome the strategy of developing and implementing a new approach to the monitoring of large audit firms. An approach that recognises that some audit firms are systematically important institutions is in the public interest. Setting out the FRC's expectations of those firms in the five areas identified is a useful first step, although we suggest some work may be necessary to gain agreement over the articulation of those areas. For example, we would question whether it is appropriate for any organisation to set out its expectations of another organisation's values.

In respect of this new approach, we are surprised to see the comment that the FRC 'will ensure that [it has] staff with the necessary skills, knowledge and expertise'.<sup>9</sup> We would expect the FRC to have confidence that it already has competent staff in the area of audit firm governance.

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<sup>8</sup> Strategy 2018/21 and Draft Budget and Levy Proposals 2018/19, page 12

<sup>9</sup> Ibid

### **Question 3: Do you have any comments on our key deliverables?**

Although the consultation document is not particularly clear on what the FRC considers to be its key deliverables, we have nothing further to say in this respect.

### **Question 4: Do you have any comments on our draft budget and funding requirements for 2018/19?**

Under the heading 'UK Exit from the EU', the consultation document states, in the final paragraph, 'This may have implications for our resourcing needs.'<sup>10</sup> However, the document has not clearly explained how.

The consultation document explains that an increase of 1% in the 2018/19 *overall* funding requirement is 'as a result of an additional funding requirement from the accountancy profession to cover additional work as competent authority for audit and for [the FRC's] new role in monitoring local public audit'.<sup>11</sup> We assume that these two items combine to give rise to £0.6m of costs under a new category of 'Audit firm monitoring'. It is unclear precisely what the additional costs represent (especially as early as 2018/19), and how the figure of £0.6m is allocated between new and existing activities.

We note also that a 1% increase in the 'overall funding requirement' obscures the fact that costs are budgeted to increase by approximately 2.8% over the budget for the previous period, and by approximately 5.2% over the 2018/17 forecast.

As indicated on page 13 of the consultation document, monitoring the quality of the audit of local public bodies will not commence until 2019, and the table on page 17 suggests that it will not commence until 2019/20. Therefore, it is unclear how the estimated 1% increase in overall funding will arise.

Table 1 appears to show that the costs of professional oversight of audit regulation in 2017/18 are forecast to be £0.2m (around 10%) over budget. A further increase of £0.1m is budgeted for 2018/19. There is insufficient information in the consultation document to explain why this is considered reasonable.

### **Question 5: Do you have any comments on our levy proposals for 2018/19?**

In Section Five of the document, it is stated that 'In 2019 funding for [the FRC's] new responsibilities to monitor local public audit will be provided by the relevant accountancy bodies'.<sup>12</sup> It is assumed that the relevant accountancy bodies are those RSBs recognised by the FRC to register audit firms for local audit.

The information provided is not sufficiently detailed to show the estimated impact on the accountancy professional bodies of the additional costs deemed to be in respect of 'additional work as competent authority for audit'.

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<sup>10</sup> Strategy 2018/21 and Draft Budget and Levy Proposals 2018/19, page 4

<sup>11</sup> Ibid

<sup>12</sup> Strategy 2018/21 and Draft Budget and Levy Proposals 2018/19, page 27

## Conclusion

The diagram on page 7 of the consultation document ably demonstrates how the FRC's mission and objectives will give rise to the desired outcomes, through transparency and integrity. The outcomes are founded on confidence and trust.<sup>13</sup> As stated earlier in this consultation response, confidence and trust in business must rely heavily upon integrity, which must be evident. Confidence and trust in business will be much easier to achieve if there is confidence and trust in the regulatory framework, including the governance of the UK competent authority for statutory audit. Therefore, we welcomed the FRC's independent effectiveness survey in 2017, and we are optimistic that the concerns expressed by respondents will be fully addressed by the FRC.

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<sup>13</sup> On page 7 of the consultation document, the outcomes are articulated as: 'Confident investors, sound decisions, effective capital markets, enhanced trust in business'.