



8 May 2013

Our ref: ICAEW Rep 71/13

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Dear Steven

**Invitation to Comment: Revision to ISA (UK and Ireland) 700 *Requiring the auditor's report to address risks of material misstatement, materiality and a summary of the audit scope* (For audits of entities that report on how they have applied the UK Corporate Governance Code)**

ICAEW is pleased to respond to your request for comments on the FRC's Invitation to Comment Revision to ISA (UK and Ireland) 700 *Requiring the auditor's report to address risks of material misstatement, materiality and a summary of the audit scope* (For audits of entities that report on how they have applied the UK Corporate Governance Code).

Please contact me should you wish to discuss any of the points raised in the attached response.

Yours sincerely

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## ICAEW REPRESENTATION

**INVITATION TO COMMENT: REVISION TO ISA (UK AND IRELAND) 700 REQUIRING THE AUDITOR'S REPORT TO ADDRESS RISKS OF MATERIAL MISSTATEMENT, MATERIALITY AND A SUMMARY OF THE AUDIT SCOPE (FOR AUDITS OF ENTITIES THAT REPORT ON HOW THEY HAVE APPLIED THE UK CORPORATE GOVERNANCE CODE)**

**Memorandum of comment submitted in May 2013 by ICAEW, in response to the FRC's Invitation to Comment: Revision to ISA (UK and Ireland) 700 *Requiring the auditor's report to address risks of material misstatement, materiality and a summary of the audit scope (For audits of entities that report on how they have applied the UK Corporate Governance Code)* published in February 2013**

<b>Contents</b>	<b>Paragraph</b>
Introduction	1
Who we are	2-4
Major points	5-28
Responses to specific questions	29-51

## INTRODUCTION

1. ICAEW welcomes the opportunity to comment on the **Invitation to Comment: Revision to ISA (UK and Ireland) 700 *Requiring the auditor's report to address risks of material misstatement, materiality and a summary of the audit scope (For audits of entities that report on how they have applied the UK Corporate Governance Code)*** published by the FRC in April 2013, a copy of which is available from this [link](#).

## WHO WE ARE

2. ICAEW is a world-leading professional accountancy body. We operate under a Royal Charter, working in the public interest. ICAEW's regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the UK Financial Reporting Council. We provide leadership and practical support to over 140,000 member chartered accountants in more than 160 countries, working with governments, regulators and industry in order to ensure that the highest standards are maintained.
3. ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.
4. The Audit and Assurance Faculty is a leading authority on external audit and other assurance activities and is recognised internationally as a source of expertise on audit issues. It is responsible for technical audit and assurance submissions on behalf of ICAEW as a whole. The faculty membership consists of around 7,500 members drawn from practising firms and organisations of all sizes from both the private and public sectors. Members receive a range of services including the monthly Audit & Beyond newsletter.

## MAJOR POINTS

5. Our major points cover the following areas:
  - **Auditor reporting needs to change, but the FRC needs to take a holistic approach to satisfying the information needs of investors and other stakeholders:** improved auditor reporting will help deal with investor dissatisfaction with corporate information but the FRC needs to address other relevant issues such as auditor involvement with preliminary announcements, communications between investors and audit committees, and safe harbour provisions. We are very keen to help develop thinking and with the implementation of proposals to address the information needs of stakeholders;
  - **Regulatory impact assessment:** we strongly believe that the FRC should develop a regulatory impact assessment framework and use this to analyse these and other proposals prior to exposure;
  - **The keys to high quality auditor reporting:** more reporting of auditor outputs is required, ie, on auditor responses to assessed risks and how auditors exercised their judgement;
  - **There are different stakeholder views:** preparers, auditors and investors all have different concerns about these proposals;
  - **The regulatory approach will determine the value of enhanced auditor reporting:** regulator behaviour drives auditor behaviour in this area, as in many others; and

- **The proposed effective date:** the extent of change proposed for one effective date is a lot to ask.

### Auditor reporting needs to change, but the FRC needs to take a holistic approach to satisfying the information needs of investors and other stakeholders

6. We welcome proposals to change the way auditors report. There have been periodic calls over many years for enhanced auditor reporting, narrative reporting and real-time reporting among other things but it now seems that there is a willingness to overcome the obstacles that have to date prevented change. Auditor liability and client confidentiality issues have not gone away but it seems that they can now be managed so that real change in auditor reporting can take place. Auditor reporting needs to change and this is the right time to make that change.
7. Investors and other stakeholders are rightly demanding more of both preparers and auditors. A willingness to accommodate these demands is critical to the restoration of trust in directors and corporate reporting and in auditors and auditing, but there is no silver bullet that will remedy investor dissatisfaction with corporate information. Changes to auditor reporting are important but auditor reporting cannot compensate for deficiencies in financial reporting frameworks and practices. For the FRC to influence effectively this debate internationally, it needs to take a more holistic view of the reporting landscape by addressing weaknesses in financial reporting and auditor reporting together. It should also address difficult areas such as auditor involvement in preliminary announcements, the desire among some investors to ask questions of external auditors directly, communications between investors and audit committees and the need for safe harbour provisions.
8. The FRC should lead the international debate by example and by using its powers of persuasion. ICAEW has long supported ISAs and we remain opposed to gold-plating. The FRC seems likely to go it alone on audit reports, as it has done recently with other information in ISA 720, banning direct assistance by internal auditors in ISA 620 and in its proposals on going concern. In our 8 October 2012 response to IAASB's Invitation to Comment *Improving the Auditor's Report*, ([ICAEW Rep 152/12](#)) we suggested that it would be helpful if the IAASB were to draft an ISA that accommodates local requirements by allowing flexibility in applying the agreed framework in a consistent manner at a national level. We noted then and re-iterate now the need to avoid two sets of requirements in the European Union (EU) and we urge the FRC to ensure that its proposals are compatible with ISAs and EU requirements.
9. There has been much discussion of the need for 'hooks' to enable institutional investors to ask more questions of audit committees. Our conversations with institutional investors indicate that they want improved access to audit committee chairs and the FRC needs to be more ambitious in facilitating this. If an investor-audit committee dialogue is not fostered, there is a risk that existing frustrations with information provided by management, and the associated lack of trust in directors, will simply be transferred to audit committees. The FRC should avoid raising expectations about investor satisfaction that may not be met.
10. No mention has been made of the needs of increasingly well-organised retail investors. The FRC needs to think creatively, and long-term about this issue. We understand that the oft-touted Australian model whereby investors are permitted to ask questions of auditors at AGMs has not, perhaps understandably, given the public space in which AGMs take place, led to the sort of 'lively debate with auditors' that some might have hoped for.
11. Changes of this magnitude cannot be experimental. Once the FRC has embarked on this path, it will be impossible to retrace its steps and there are bound to be unforeseen and unintended consequences. We hope that the FRC will monitor the application of any new requirements closely and be ready and willing to react should outcomes not be as expected.
12. In our 8 October 2012 response to IAASB noted above, we suggested that while there have been significant developments in corporate reporting and governance, the audit report has stayed the same, and that the time for change has come. We also noted that change needs to

be undertaken in tandem with other stakeholders, including accounting standard-setters, and that auditors alone cannot solve all of the problems in the financial reporting chain.

13. We would be pleased to hear about the links the FRC has made between this project and projects being undertaken on the financial reporting side, and to be reassured that the FRC is not taking a piecemeal approach to these issues.

#### ICAEW's contribution to the auditor reporting debate

14. ICAEW has long recognised the need for better quality auditor reporting. In January 2007, we published *Auditor Reporting* as part of our Audit Quality Forum *Fundamentals* series.

That report noted among other things that:

- the readability of audit reports would be improved by moving the opinion to the front and much of the standardised boilerplate text to the back, or to an appendix;
  - investors require more company-specific information on key subjective areas;
  - there is a need for a further debate with all key stakeholders on the provision by auditors of company-specific information in the audit report, including significant and particularly subjective audit issues; and
  - audit committees might be required to disclose in their report to shareholders, key issues and significant accounting and reporting matters discussed with auditors as a result of the audit. The auditor's reporting role in relation to these disclosures would need to be considered.
15. All of these issues remain relevant to the current proposals. The working group recommended that the DTI (now BIS), the FRC and other UK stakeholders encourage the IAASB, the EC and other European bodies to consider the recommendations above, especially in discussions regarding the development of ISA 700 and the common audit report.

#### Regulatory Impact Assessment

16. The FRC makes central to this consultation, respondents' views on the regulatory impact. We strongly believe that the FRC should perform some analysis **before** it releases exposure drafts for them to be legitimate and for assertions regarding their impact on audit quality to have any credibility. We noted in our 15 March 2013 response to IAASB on its ISA 720 exposure ([ICAEW Rep 44/13](#)), a draft of which was copied to the FRC, the fact that we do not believe that IAASB can legitimately continue to ask questions about impact unless it too makes some effort, however small, to include some analysis in its proposals. Absent any sort of analysis or evidence, a 'belief' that costs will exceed benefits is uninformed speculation. It is not enough to support major changes such as these.
17. We also noted that we fully recognise the time, costs and the challenges involved in developing metrics for these analyses which need to be built into standard-setters' work programs. Getting the proposals right the first time by performing these analyses is preferable to asking practitioners to bear the costs by finding out through implementation that proposals are not workable. We said that absent such analyses, we did not believe that IAASB can or should pronounce on, or ask respondents about, whether the public interest is likely to be served.
18. The same considerations apply to FRC's questions on costs, benefits and other impacts. If the FRC is not prepared or is unable to provide either evidence regarding costs, benefits and other impacts, or at least a framework for the measurement or description of costs, benefits and impacts it is not in a position to ask to respondents to do so. We urge the FRC to develop a framework to describe and measure the costs, benefits and impacts of all of its proposals.

19. Discussions on costs often involve the word 'should'. Many believe that these proposals should not cost much because the information to be reported by auditors is already available. The fact is that these proposals will increase audit costs, regardless of whether they 'should', because of concerns about liability, the need to take a great deal of care over the wording of disclosures, and because of the likely downward pressure on materiality levels. Some investors have indicated that they are happy to bear these costs. They are not great in the overall scheme of things. But in other cases, and particularly with smaller entities, there will be resistance to cost increases and auditors will absorb the costs. Rightly or wrongly, it is inevitable that in some cases the effect will be boilerplate disclosures and a reallocation of resources from elsewhere in the audit, to pay for what may be perceived as a compliance exercise. This will not improve audit quality overall. The FRC should admit that there are costs involved and encourage audit committees to justify those increased costs to management.

### The keys to high quality auditor reporting

20. The proposals would be improved if there were greater focus on the reporting of responses to assessed risks and to areas involving judgement, ie, outputs. The FRC has focussed on the disclosure of auditor inputs and processes which is fine as far as it goes, but which leaves too many questions unanswered. The disclosure of materiality levels will have a novelty value for a year of so but, absent a discussion of the judgements and thought processes that led to the figures reported, the disclosures will be largely meaningless.
21. Investors are particularly concerned that auditors should use their judgement to determine which risks are significant for reporting purposes. 'Significant risks' identified during the planning and execution of the audit should not be mapped to disclosures in the audit report. The FRC has considered the criteria for determining what should be reported, but more consideration needs to be given to which risks to **exclude**. This is much harder, but it is important, because the default position will be 'all of them'. We note elsewhere in this response the need for regulators to curb any tendency to encourage auditors to include more rather than less for the avoidance of doubt. The FRC must ensure that AQRT inspectors do not discourage the use of judgement by auditors by constantly challenging auditors regarding matters that were excluded.
22. Investors also note the possibility of reporting requirements driving the assessment of significant risks during the planning and execution of audits. If everything that is assessed as significant is eventually reported, because regulators always challenge non-reporting, rightly or wrongly, there will be a behavioural impact and auditors may be less willing to assess a matter as significant. It is therefore critical that auditors are permitted to use their judgement in determining what to report.
23. We note in our answer to question 10 below, that we do not believe that the illustrative disclosures in section 3 provide good examples of how audit scope was responsive to the auditor's assessment of risks and materiality. The disclosures are a list of figures, not very informative, not very interesting and they will inevitably lead to further questions, about which locations were visited, why, and why materiality levels have changed, for example.
24. It is inevitable that anything auditors say about companies that does not simply repeat information already provided can be construed as 'original' information. Many believe that auditors should not provide such information. An explanation and examples of what directors might typically say about a matter in the financial statements and what auditors might reasonably say about the same issue in some relatively simple areas, such as litigation, going concern and the valuation of financial instruments, would be enormously helpful to both preparers and auditors, even if they are not included in the standard. In the case of significant litigation for example – is the FRC expecting auditors to comment on their assessment of the likely outcome of the litigation? Or is it expecting auditors only to comment on the process it went through to arrive at that assessment? Is the latter information useful?

## There are different stakeholder views

**25.** Our members include preparers, auditors and investors. They have different ‘takes’ on these matters, and groups do not necessarily agree among themselves. Auditors are concerned, for example that requirements to disclose details of materiality levels are not only of little value, particularly as described in the proposals, but that they will compromise their ability to conduct audits effectively because frauds may be deliberately engineered around these figures. They also fear that they will be forced into a default position of disclosing everything they can, rather than risk having their judgement regarding what to exclude, challenged by preparers, investors and regulators. Preparers are concerned that their right and duty to provide entity-specific information will be compromised by the disclosure of audit risks which will overlap with management disclosures. They are also concerned about the extent to which investors, who are in a much better position to question directors than they are auditors, will seek explanations from directors about what auditors have said, and worry about wording differences between preparer and auditor accounts of the same issues. Investors have concerns that disclosures will quickly become boilerplate. While similar disclosures year-on-year within an entity might be expected when little changes, investors will be particularly concerned if auditors and preparers also seek to align their positions, and different entities in the same sector seek to align disclosures. All of these are legitimate concerns. Few of them are addressed by the FRC’s proposals.

## The regulatory approach will determine the value of enhanced auditor reporting

**26.** Regulatory activity drives auditor behaviour. The manner in which AQRT inspectors approach disclosures in auditors’ reports will have a significant effect on their quality. Challenging auditor judgements is healthy but any pressure on auditors to disclose additional matters ‘for completeness’, or ‘for the avoidance of doubt’ or other encouragement of ‘more rather than less’, which is a common regulatory approach, will simply accelerate the degeneration of disclosures into boilerplate. The opportunity will arise to challenge the inclusion of disclosures as unnecessary, and the FRC should encourage AQRT inspectors to actively consider this possibility.

## The proposed effective date

**27.** All of those we have discussed these proposals with, preparers, investors and auditors alike believe that the extent of change proposed for one effective date is a lot to ask. We understand that the proposed date is intended to implement on a ‘big bang’ basis:

- enhanced audit committee reporting;
- the Sharman proposals on going concern reporting; and
- other changes to the UK Corporate Governance Code.

**28.** If the FRC wants the proposals to be implemented properly, it must either postpone them for a year, say, or stagger them. Stakeholders from many constituencies will urge the FRC to consider later or staggered implementation, for a variety of reasons. If the FRC goes ahead anyway, it must accept that while preparers and auditors will do their best to implement such requirements as are in force, without time to make thorough preparations or conduct dry runs, the quality of reporting all round will not be good as it could or should be. All concerned will be urged by lawyers among others, to say as little as possible while complying with the letter of the requirements. Such defensive reporting will set a precedent which will not impress investors.

## RESPONSES TO SPECIFIC QUESTIONS

### Overall view

**Question 1: Do you agree that the auditor's report should include a description of the auditor's assessed risks of material misstatement, materiality and the audit scope? If not, why not?**

29. We agree that the auditor's report should include some description of the auditor's assessed risks of material misstatement but we do not believe that the proposed descriptions of materiality and audit scope, or the examples thereof, are adequate. Furthermore, we believe that more work is needed on the proposed requirements relating to audit risk if it they are to be useful. The examples provided are broad, but they lack depth and quality.
30. The continuing debates at IAASB concerning the nature and extent of auditor disclosures are ponderous, but they reflect the importance of these changes. If the disclosures made are seen as boilerplate and of little value to investors in a specific sector or more generally, the project as a whole will have failed.
31. Our discussions with investors indicate their interest in:
  - Those assessed risks of material misstatement that 'keep auditors awake at night', ie, the 'key' risks, and how auditors addressed them. These are not necessarily the risks that had the greatest effect on overall strategy, or indeed to which audit resources were directed. Much audit resource is devoted to routine areas on the audit of IT systems, and entities engaging in low-risk activities. All of this must be covered, but it is of less interest to investors. Some critical audit risks, such as litigation, have, when the audit bill is added up, a relatively small amount of resource allocated to them even though they represent a large amount of partner time; and
  - The scope of the audit, particularly the extent that it represents the auditor's **response** to the key risks noted above.

**Question 2: Do you agree that these proposals should be limited to entities that explain how they comply with the Code? If not, why not?**

32. We agree that these proposals should be limited to entities that explain how they comply with the Code. Some investors believe that the proposals should also be applied to AIM companies but the FRC needs to be aware in any case of the potential unintended consequences of relentlessly raising the bar. Not long ago, there was widespread acceptance that regulation probably had a marginal effect if any on the decision of entities to seek capital market listings and that once listed, entities would rarely if ever de-list. Things have changed and the FRC has a duty to be mindful of the long-term effects of its decisions on UK businesses and capital markets.

### Question 3:

**(a) Do you consider that the provision of such information by the auditor will be of benefit to shareholders and other users of the financial statements and, if so, can you explain what those benefits would be and how they would arise?**

33. We note in our major comments above our strongly-held belief that the FRC must, if it cannot provide evidence to support its implicit assertion that its proposals will benefit shareholders, at the very least provide a framework for respondents when asking questions such as these. While in principle the time is now right for auditor reporting to change, we are concerned that these proposals have not been thought through properly. It would be a shame if shareholders were denied the benefit of better auditor disclosures because the FRC acted in haste.



**(b) Do you believe such information would provide an effective ‘hook’ for investors and other users to start a dialogue with the company about the audit?**

**34.** We find it odd, and slightly worrying, that the FRC expects investors to seek a dialogue with the company about the **audit**. Are audit committees realistically going to be able to provide investors with satisfactory answers about why the auditors’ materiality levels were reduced by x% in the current period? Is it right that they should be presented with such questions? Investors are mainly concerned about the audit to the extent that auditor responses to assessed risks signpost issues regarding the company. Investors should seek to use the information provided by auditors to seek a dialogue about the company as well as the audit. Unfortunately, as it stands, the information provided is only likely to help them do this in part because, as we note in our major points above, it is focussed on audit inputs and process rather than outputs.

**Question 4: Do you believe that directors are likely to disclose information about the audit (of the type that would be required in accordance with these proposals) under the September 2012 changes to the Code? Is it more appropriate for such information to be provided in the auditor’s report or by the board in the section of the annual report addressing the work of the audit committee, and why?**

**35.** Good directors might disclose information about the audit in the manner suggested, but investors are likely to be less concerned by such entities that already provide good quality, trusted information. We think it very unlikely that all directors would be persuaded to disclose information about the audit in accordance with these proposals, and we think it highly likely that they would argue that it is not appropriate for such information to be provided by audit committees.

## **Assessed risks of material misstatement**

**Question 5: What do you believe would be, if any, the benefits, costs and other impacts of the proposed requirement to describe in the auditor’s report certain risks of material misstatement that were identified by the auditor?**

- 36.** We note in our major points above our strongly-held belief that the FRC must, if it cannot provide evidence to support its implicit assertion that its proposals will benefit shareholders, at the very least provide a framework for respondents when asking questions such as these.
- 37.** There will be costs associated with the disclosure of audit risks. The behavioural dynamics of any change in standards mean that more partner, manager and company management time will be taken up considering the new requirements and discussing the disclosure of audit risks on an on-going basis. Lawyers will be involved.

**Question 6: Do you agree that the basis for determining the risks of material misstatement to be described in the auditor’s report (see proposed paragraph 16A(a) of ISA (UK&I) 700) is appropriate?**

- 38.** Investors want to know what additional work has been performed in respect of each significant risk. They want to know what is important to auditors, the scope of the work in specific areas, where the work was focussed and the issues arising. The illustrative examples in the papers that were presented to the IAASB’s April 2013 meeting<sup>1</sup> meet these criteria more closely than the FRC’s proposals.
- 39.** The proposed basis for determining the risks of material misstatement to be described in the auditor’s report in paragraph 16 (a) are those risks that ‘have the greatest effect on overall audit strategy and the allocation of audit resources’. We have not formed a view as to whether the risks that should be disclosed are ‘significant risks’ as described in the ISAs, ‘key matters

<sup>1</sup> [www.ifac.org/sites/default/files/meetings/files/20130415-IAASB-Agenda\\_Item\\_2A-Illustrative\\_Auditors\\_Reports-final.pdf](http://www.ifac.org/sites/default/files/meetings/files/20130415-IAASB-Agenda_Item_2A-Illustrative_Auditors_Reports-final.pdf)

of audit significance', 'key audit matters' or similar as described in IAASB's current deliberations. But we note in our answer to question 1 above, that investors are more concerned with the risks that keep auditors awake at night. These are not necessarily the risks that had the greatest effect on overall strategy, or indeed to which audit resource was directed. IAASB's extended consideration of this issue is important.

**Question 7: The risks disclosed by the auditor in complying with proposed paragraph 16A(a) of ISA (UK&I) 700 may well differ from the principal risks disclosed by the directors in the business review in the annual report. What are your views about this possibility?**

40. Investors recognise that audit risks are not the same as business risks. If auditors and directors map the risks across in a 'mirror image' exercise, investors will be justifiably disappointed. Business and audit risks overlap, but they are not the same thing and investors will welcome the different perspectives. Many risks disclosed by entities are likely to be non-financial risks such as reputational risks, that only become financial risks when things go wrong. However, audit committees are likely to be called on to explain to investors why auditors have reported some risks and not others. We note in our major comments above the need for the FRC to take a more holistic approach to investor dissatisfaction with corporate information, particularly with regard to communications between audit committees and investors.

**Question 8: Do you believe that the omission from the auditor's report of a particular risk of material misstatement would pose a threat of significant loss or damage to the auditor if, after the event, it became evident that the risk had given rise to significant damage to the company?**

41. It is possible that attempts will be made by third parties to seek redress from auditors if an omission from the auditor's report of a particular risk gives rise to significant damage to the company. We do not think that this is a proper issue for standard-setters to take account of in developing standards.

## **Materiality**

**Question 9: How do you assess the benefits, costs and other impacts of the proposed requirement to provide in the auditor's report an explanation of how the auditor applied the concept of materiality in planning and performing the audit, including specifying the threshold used by the auditor as being materiality for the financial statements as a whole, and the balance between them?**

42. We note in our major comments about our strongly-held belief that the FRC must, if it cannot provide evidence to support its implicit assertion that its proposals will benefit shareholders, at the very least provide a framework for respondents when asking questions such as these.
43. There will be costs associated with the provision of information on materiality. More partner, manager and company management time will be taken up with considering the new requirements. While less partner, manager and company management time will be taken up with discussions regarding materiality than those regarding the summary of audit scope or audit risks, the proposals are not cost-free. Including materiality measures in the audit report will drive materiality levels down, increasing the audit work that auditors are required to perform, probably without much impact on audit quality.

## **Summary of audit scope**

**Question 10: How do you assess the benefits, costs and other impacts of the proposed requirement to provide in the auditor's report a summary of the audit scope, and the balance between them? Does the illustrative disclosure in Section 3 provide a sufficient explanation of how the audit scope was responsive to the auditor's assessment of risks and materiality?**

### Illustrative disclosure in Section 3

44. We do not believe that the illustrative disclosures in section 3 provide an adequate explanation of how audit scope was **responsive** to the auditor's assessment of risks and materiality. They are a list of figures, not very informative and not very interesting. They will inevitably lead to further questions. Which locations were visited? Why? How much of an audit is a 'partial' audit? And why was the materiality level 'x' this year when it was 'y' last year? While this provides 'hooks' for investors to ask questions of audit committees about the company, it is unlikely that audit committees will be able to provide satisfactory answers regarding the audit itself.
45. The IAASB is taking a more measured approach to developing its proposals in this important area and we urge the FRC to continue to consider carefully the substance of the IAASB's deliberations.

### Benefits, costs and other impacts

46. We note in our major comments above our strongly-held belief that the FRC must, if it cannot provide evidence to support its implicit assertion that its proposals will benefit shareholders, at the very least provide a framework for respondents when asking questions such as these.
47. There will be costs associated with the provision of a summary of audit scope. More partner, manager and company management time will be taken up considering the new requirements and discussing the summary of audit scope on an on-going basis. Lawyers will be involved.
48. The requirements may lead to adverse changes in the way that auditors interact with audit committees, and indeed the way that they plan the scope of the audit, in order to achieve the 'right' number of locations visited, for example.

### Avoiding standardised language

**Question 11: Do you believe that the wording of paragraph 16A and paragraphs A9A to A9C is sufficiently principle-based so as to avoid standardised language?**

49. The FRC should seek positive outcomes, in the form of useful auditor reporting, rather than negative ones such as 'avoiding standardised language'. Avoiding standardised language is not achieved by finessing the wording of auditing standards in any case. It is achieved by a complex set of behavioural dynamics involving auditors, the companies engaging them, the regulators inspecting them and investors. Standardised language is a safe default position. It is almost inevitable that auditors and companies will seek safety by emulating both themselves and each other over a period of time, but this does not mean that the process of getting there is not worthwhile.
50. Unfortunately, for the reasons set out above, it is arguable that the wording of paragraphs 16 (a) and A9 (a) to A9 (c) will actually encourage standardised wording from the outset with, for example, the figures for materiality and locations visited being slotted into the same tables with the same standard wording every year. The main reason for this is, as noted above, is an excessive focus on the audit inputs and process (which is, after all, a process standardised by standard-setters), at the expense of outputs, i.e. audit judgements.

### Effective date

**Question 12: Do you foresee any difficulty if the effective date is periods commencing on or after 1 October 2012?**

51. We note in our major points above that the effective date is too soon, taking account of the need for companies to implement all of the other FRC proposals with the same effective date.

We suggest that if the FRC wants the proposals to be implemented properly, it either postpones the big bang implementation of these proposals for a year, or staggers them.

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