

AUDIT NEWS

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INTRODUCTION

Welcome to this winter edition of Audit News, where we report on recent changes to the Audit Regulations as a result of the Financial Reporting Council's (FRC) Auditor Regulatory Sanctions Procedure (ARSP) effective from 1 January 2014.

This edition also contains short articles on the Small Companies (Micro-Entities' Accounts) Regulations 2013; the Competition Commission report into the audit market; an alert that we have issued our helpsheet on the audit of investment business entities regulated by the FCA; and a

reminder about the mandatory course for Audit Compliance Partners.

We hope you find this edition of Audit News useful, and we would like to take this opportunity to wish you a very happy break over the holiday period.

CHANGES TO THE AUDIT REGULATIONS AS A RESULT OF THE FRC'S ARSP

The Audit Regulations have been updated with effect from 1 January 2014 to take account of the FRC Auditor Regulatory Sanctions Procedure (ARSP) which has now been published.

The changes follow from the FRC governance review in October 2011, with the agreed elements of this being enacted by Statutory Instrument (SI) 1741 in July 2012. Under article 5 of the SI, the FRC was given the power to determine sanctions against audit firms directly without reference to the recognised supervisory bodies (RSBs).

Who do these changes affect?

The sanctions regime applies to any firms that are subject to inspections by the Audit Quality Review team (AQR) of the FRC and, as these are firms that carry out significant numbers of major audits, this policy only affects a small number of firms that are registered for audit with ICAS.

What are the key changes to the Audit Regulations?

Whilst ICAS has been asked to apply the sanctions procedure by the FRC, we are doing this on behalf of the FRC and not as part of the audit regulations. The regulations have, therefore, been amended to ring fence this particular activity and establish how they operate alongside the procedures operated by ICAS.

The sanctions determined by the FRC are to be treated as

issued by ICAS itself and Chapter 7 of the Audit Regulations now sets out how this will apply in practice. This has resulted in the creation of new regulations 7.00 and 7.00A.

Regulations 6.02, 7.02, 7.03 and 7.06 have been modified to accommodate FRC findings, and to indicate how the transition between regulatory regimes might be handled. This could arise, for example, if a firm ceases handling major audits during a sanction period.

As ICAS is charged with implementing the sanctions, it follows that the enforcement regulations of the Audit Regulations continue to apply; so, for example, 7.03f has been amended, and 7.03j added, to enable the Audit Registration Committee to apply

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its own sanctions for non-compliance with sanctions levied under the ARSP.

There have also been amendments to regulations 7.16 and 7.17 to deal with regulatory penalties arising from the ARSP.

The appeal mechanism

A draft ARSP was issued in December 2012 to set out how the FRC might apply sanctions in practice and, in particular, to explain the appeal mechanisms associated with it.

The appeal mechanism should enable firms to challenge any sanction that the FRC may have applied. This appeal mechanism is operated by the FRC and is separate to the appeals system set out in Chapters 8 to 9 of the Audit Regulations and, therefore, the introduction to those chapters has been amplified to reinforce this. In addition, regulations that address appeals against sanctions have been ring fenced to decisions of the Audit Registration Committee.

Other changes

Other changes to the Audit Regulations and Guidance include:

- In July 2012, the ICAS council agreed to amend the definition of audit affiliate, changing the term from 'regulated non-member' to 'affiliate' and this change has now been reflected in this recent version of the regulations. In addition the term 'byelaws' has been amended to reflect the fact that the requirements in ICAS are now set out in Regulations instead of Byelaws;
- The Professional Oversight Board has been changed to the Financial Reporting Council;
- The Audit Inspection Unit is now called the Audit Quality Review team;
- The Financial Services Authority is now the Financial Conduct Authority.
- In the case of CPD, guidance has been added to regulation 3.17 to the effect that where individuals are registered themselves with one regulatory body, but their firms with another, then the most demanding CPD regulations of either body apply.

The most up to date Audit Regulations can be accessed on the ICAS website at: icas.org.uk/Audit_Regulation.aspx

SMALL COMPANIES (MICRO-ENTITIES' ACCOUNTS) REGULATIONS 2013

Following a process of consultation, the UK Government has confirmed the approval of the Small Companies (Micro-Entities' Accounts) Regulations 2013.

The Government response to the consultation process can be accessed at: gov.uk/government/uploads/system/uploads/attachment_data/file/237045/bis-13-1124-simpler-financial-reporting-for-micro-entities.pdf

The Regulations apply to a small company which:

- If, in its first year, satisfies two out of three of the criteria noted below; and
- For subsequent years, if it meets the qualifying criteria in two consecutive financial years.

A micro-entity is defined as an entity meeting two of the three following criteria:

- Balance sheet total of less than £316,000;
- Net turnover less than £632,000; and
- Average number of employees during the financial year: 10 (or fewer).

What are the key aspects of the Micro-Entities' Regulations?

The financial reporting rules for micro-entities enable such entities to draw up an abridged profit and loss account and

balance sheet. Companies will be required to file the abridged balance sheet at Companies House, but do not have to file a profit and loss account. The notes to the accounts of a micro entity will not be required with the exception of details of any outstanding commitments by way of guarantees, and advances and credits to directors.

The Department for Business, Innovation and Skills (BIS) has said that the new rules, which are optional, will apply retrospectively for financial years ending on or after 30 September 2013, provided the accounts are filed on or after the necessary regulations have come into force.

The relaxations will not apply to charities or other obvious exclusions, such as public companies. Limited Liability Partnerships will also be excluded from using these exemptions for the time being.

The exemptions are optional and it will be for owners and directors of micro-entities to assess the possible effect of reduced disclosures on their company and to decide which form of financial reporting statement – micro, small or full – best meets their company's needs.

The Regulations can be accessed at the following webpage: legislation.gov.uk/ukdsi/2013/9780111105207

COMPETITION COMMISSION REPORT INTO THE AUDIT MARKET

On 17 October 2013 the Competition Commission (CC) issued its final report on its inquiry into the FTSE 350 audit market.

The CC's main conclusion was that audit appointments in respect of FTSE 350 companies should be subject to mandatory re-tendering every 10 years.

It is noted that this is a significant change from their provisional remedy of mandatory re-tendering every 5 years, and this reflects strong concerns from the FRC, companies, and investors that a shorter interval would have risked undermining the intensity of competition and audit quality.

The CC further concluded that:

- The FRC's Audit Quality Review (AQR) team should review every audit engagement of companies in the FTSE 350 every 5 years, with the findings and grade to be reported to shareholders;
- There should be increased accountability of the auditor to the Audit Committee;
- There should be a shareholder advisory vote on the annual Audit Committee Report;
- The FRC should be given a secondary objective to have due regard to competition; and
- So-called 'Big 4' clauses in loan agreements should be prohibited.

Further information can be found on the Competition Commission's website: <http://www.competition-commission.org.uk/>

ICAS HELPSHEET – THE AUDIT OF INVESTMENT BUSINESS ENTITIES REGULATED BY THE FCA

In our previous two editions of Audit News we announced that we had issued helpsheets for the audit of specialist and regulated entities, including charities registered with OSCR and The Charity Commission in England and Wales; pension schemes; Registered Social Landlords; and Credit Unions.

When we issued our Audit Monitoring Annual Report 2012 at the start of this year we noted that many of the audit files in 2012 that were identified as being of poorer quality were of a specialist or regulated nature. As a result, we strongly advise firms to ensure that Responsible Individuals who have responsibility over such clients are undertaking regular training in the relevant area; that audit procedures reflect the specialist

aspects of the assignment; and that sufficient time is devoted to these audits, which can often be perceived to be of a 'smaller' nature.

Helpsheet for the audit of investment business entities regulated by the FCA

We have now issued a helpsheet on the audit of the audit of investment business entities regulated by the FCA.

All of our helpsheets are available to ICAS members on the ICAS website, at icas.org.uk/regulation/news/helpsheets/



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REMINDER – MANDATORY COURSE FOR AUDIT COMPLIANCE PARTNERS

Keeping Your Audit Firm and Files on the Right Track

As we confirm in each of our Audit News editions, these courses are mandatory for Audit Compliance Partners, however to ensure mandatory attendance is not too onerous, you are required to attend only once every five years, and the courses are still heavily discounted for those requiring mandatory attendance. Courses are developed and delivered

by the ICAS Audit Monitoring team and dates for 2014 will shortly be confirmed and able to be accessed at: icas.org.uk/Businesscourses/

If you would like to see any particular articles in future editions of Audit News or any particular auditing areas covered in future monitoring helpsheets please send your ideas to: auditandpracticemonitoring@icas.org.uk

