Independent Review into the Quality and Effectiveness of Audit. Response by Baroness Bowles

This is a personal response based on my policy and legislative involvement in company law and International Financial Reporting Standards (IFRS), including as an MEP from 2005 to 2014, serving throughout on both the Legal Affairs Committee and Economic and Monetary Affairs Committee and chairing the latter from 2009 to 2014. I was a major contributor to the EU consultations and legislation concerning company law, audit and accounting. Since then I have continued to research and engaged on these issues with regard to policy and legislation.

I hold company directorships which are included in the House of Lords Register of Interests. I have no objection to the publication of my submission under my name.

Introduction - Company Law and International Standards

The call for views asks in particular in paragraph 86 for comment regarding support for the primacy of law in the context of distributions. The issue of divergence of standards from company law is one that I have investigated at some length and it has relevance to several questions in this review and to culture. There are two existing belief systems: one side that takes a company law belief and says those are the supreme rules – and it is not surprising that lawmakers tend to that view – and others that consider international financial reporting standards (IFRS) are a more accurate and certain way to achieve compliance. In general the large accounting firms are in the second camp and so have been the FRC and parts of BEIS (and its predecessors). Past attempts to amend company law to match reporting standards failed, largely at the hand of Parliament.

International standards have diverged from company law, simply because standards are the 'common denominator' for the 140+ different countries that follow IFRS and the specifics of company laws for each country cannot therefore be covered, as explained by an IASB board member in an article[1] in February this year following the AssetCo decision.

The evidence I found in FOIs and other documents, and which I submitted to the Kingman Independent Inquiry[2], clearly showed the regulator and officials in the department of business orchestrating opinion with the ICAEW, Big 4, 100 group and the IASB to 'ensure we get the profession and corporates on our side' when there was challenge by investors over the matter of distributions. This was reinforcing that belief system. The 'beliefs' matter is wider than distributions, covering true and fair and straying into what auditors are expected to do and why it is mentioned in my responses to many questions.

[1] https://www.ifrs.org/news-and-events/2019/02/returns-reinvestment-opportunities-and-dividend-distribution/
[2] A copy of my submission is supplied for reference and further elaboration in Q4

Slowly there has been some coming round to acknowledging that the law must prevail over standards when circumstances give rise to a difference. This imperative has now been roundly confirmed at least as regards 'true and fair view'[3]. Where there is still reticence, even evasion, including in response to Parliamentary Questions, is over the matter of distributions where the law is clear about not including unrealised profits but questions seeking clarification vis a vis standards are sidestepped by saying the law does not require separate elaboration[4] of what is distributable and what is not, which is the obfuscation that was created from the FRC side in the QC 'battle of legal Opinions'[5]. The point is not the elaboration, but what happens and what is checked by auditors.

We seem to have got stuck in this dual belief situation largely because the UK (and Ireland who share the same standards) are unique in using IFRS at the individual company level, and also in having modified UKGAAP to import IFRS provisions, without replicating the prudence requirements in company law. There was a strong lobby not to have to fulfil two sets of requirements for company and group level, including by the regulator[6].

The EU allowed this national application of IFRS at company level (rather than just for group accounts) as an **option** after extensive lobbying and insistence by the UK and UK based profession. Only UK and Ireland (both under the FRC) permitted company level IFRS. Other IFRS-using countries have made significant modifications (eg Australia and Japan) and/or apply it in conjunction with a solvency test that bridges the difference (eg Australia, Canada and New Zealand)[7].

That does not make all accounts and distributions wrong, for example a judicious approach to dividend distribution may compensate for any unrealised profit that is included by virtue of the standards. Nevertheless it is extraordinary the way the debate around this matter has been conducted and it is one of the reasons that prompted me to investigate, which in turn led to other evidence about culture, regulatory and cognitive capture that I submitted in my responses to the Kingman Inquiry and the CMA.

I do hold the view that the law must prevail, and that ultimately judges will establish that if cases get to court. There is some indication of that in recent judgements although very few cases get to trial owing to settlement. There is a lot of wisdom in the simple and forward-looking prudence of company law that by relegation to 'defunct' in the practiced standards belief system has meant we are now looking for ways to re-invent forward-looking measures. Therefore whatever solutions this inquiry suggests, an element of 'back to the future' already seems intrinsic, whether that is recognised or not.

[3] HL 5280, Hansard 12 March 2019 column 212GC and call for views footnote 13
[4] HL 5280
[5] BEIS select Committee Report reference 156 on page 26
[6] Visits to my office in the European Parliament and FRC letter of 8 April 2005 (see Q4)
[7] BEIS Government response: Insolvency and Corporate Governance pp 19-20

Response to Questions

Chapter 1 - Definitions of Audit and its uses

Q1: For whose benefit should audit be conducted? How is it of value to users?

This is a key question. As quoted in the foreword tens of millions of people rely upon audit. The BEIS select committee report 'The future of audit' highlights how employees, pensioners, suppliers and taxpayers have been affected by company failures that have rapidly followed on from an audit 'all clear'. At a basic moral level this indicates that audit must serve those people, the public interest. Additionally if audited accounts are required to be filed and publicly available, it is a logical conclusion that the public is entitled to be a 'user'.

The Kingman review refers to 'users of accounts' and in that report there is emphasis on 'consumers and users not producers'. The consumers and users must include the public if the protection of the interests of the wider public is to have effect. 'Producers' must largely reference the accounting, audit and standard setting community which has held sway for so long over the way things are.

At a recent meeting on audit under Chatham House rules I asked 'who is audit for?' One senior asset manager said 'Primary investors are not qualified to 'use' financial statements'. 'The ability to raise capital is driven by professionals and the man in the street can't understand'.

A distinguished FTSE chairman, former big 4 partner and former CFO said 'The financial reports are for institutional shareholders'. 'Ordinary shareholders only look at the chairman's report, remuneration and maybe other bits they are interested in. They can't 'consume' the accounts'.

It may be true that is how it is at present, but is it how it is meant to be or should be? I think not.

Ordinary investors (and indeed the public) are the target of the provisions in company law, which are for the protection of the public with respect to companies. That protection is part of an implicit bargain with society for the granting of the benefits of incorporation and limited liability. It is a bargain that gives freedom for entrepreneurial spirit without fear of personal ruin, as elaborated by Andy Haldane[8] in 2015 as he traced the path through early incorporation and limited liability. Publication of accounts and audit are part of that protection for the public interest.

[8] Andy Haldane Speech May 2015 'Who owns a company?'

That company law provisions such as true and fair are for the ordinary investor has been made clear during the RBS Rights Issue trial[9]. The issue at stake was what was 'necessary information' to be included in the prospectus for the purposes of section 87A(2) FSMA to 'enable investors to make an informed assessment of….. the assets and liabilities, financial position, profits and losses, and prospects' of RBS. Refusing permission to admit further expert evidence of an equity analyst Mr Justice Hildyard said, at paragraph 54:

> "***even if evidence from equity analysts might assist in determining what equity analysts would agree to be a minimum standard of the information to be included in a prospectus, that standard would not necessarily be, or even be likely to be, an appropriate one for the ordinary investor whose protection is the statutory objective. Similarly, I share the related concern that such evidence might obscure the test and skew, rather than correctly guide, the Court's approach."***

The judgement is relevant to consideration of audit because the recitation about prospectuses appears almost identically in s393A of CA06, that the accounts must give a 'true and fair view of the assets, liabilities, financial position and profit or loss'. Thus it seems that the law by any reasonable construction is that accounts/financial statements and audit assurance must be for the ordinary investor.

Also, rather vitally, the judgement notes that paying attention to the evidence of experts can obscure or skew, rather than correctly guide, the approach that has to be taken. This is an important lesson for accounting and audit which seems to have lost its way in this respect. It is important for recognising that in serving 'users' it is the ordinary investor (alongside public interest) who is paramount, not the expert users.

In the world of accounts, auditing and standard setting it tends to be only the voices of experts that are heard and considered. Further, although Sir John Kingman said in his report that it is the usual way in the UK for regulators to set standards, the accounting and audit industry is unique in that there is no or minimal separation of the profession from the standards. Financial services standards are set more by central bankers than bankers, by market regulators not dealers. Yet accounting standard setting is almost entirely contained in bodies and regulators dominated by the accounting profession. It is further unusual for one regulator to have both accounting and auditing, which may not have helped in the process-led rather than sceptical and judgement-led approach to audit that has been allowed to develop.

[9] *http://www.bailii.org/ew/cases/EWHC/Ch/2015/3433.html* see paragraph 54

As already pointed out[10] IFRS does not take account of company law yet it is company law, the statute not standards, which define the protection for the ordinary investor and public. A lot of what is sought can be achieved by going 'back to the future' and delivering audit according to statute, removing the jargon of IFRS and 'financial statements' and delivering strictly and directly on all of the statutory provisions. Audit under statute is intended to be for the company (and especially the ordinary investor) and the public interest: adding in concern for sophisticated or expert users must not skew the requirements to the detriment of the information for the main users – that is the lesson of the RBS case.

Value is clear – that the accounts and books (including controls) are in order and no material errors found. Simplicity of the pass/fail can be viewed as for the ordinary investor, they are the prime recipient not professional users, and what has to be verified to give that pass/fail is precious and should be rigorously applied.

Q2: Should the audit be designed to enhance the degree of confidence of intended users in the entity or just in the financial statements?

Audit should lead to confidence in the entity as a whole regarding its financial position and safeguards for the future such as going concern, viability, preservation of capital.

The public and investors are also becoming interested in more than financial statements (but see also Q7) as evidenced by the repeated need to enhance corporate reporting, such as by introducing the strategy report, section 172 reports, pay, gender balance and supplier payment reporting. Experience seems to show that governance is often not done sufficiently well until reports are required. Consequentially there is public scepticism about unverified KPIs. The public scepticism is a reflection of the type of scepticism that they expect from auditors and a sceptical appraisal should be applied to all reporting. The regulator is only just extending cover to the whole of the annual report and there is a case to say wait and see what that brings. In the past the FRC has said that it was powerless to address issues such as the details in the strategic report when raised by NGOs. If/when independent verification is required of non-financial matters it should not be part of the statutory audit and is probably best performed by other organisations.

Q3: Should UK law be amended to provide greater clarity regarding the purpose of an audit, and for whom it is conducted? If so, in what way?

It should be put beyond doubt that the public interest and ordinary investor is at the core of audit. This should include a direct requirement for auditors to act in the public interest, rather than considering that they 'fulfil a public interest role' as it is often put. This naturally leads to matters such as cautionary disclosures and alerts. It is a failing in the

[10] https://www.ifrs.org/news-and-events/2019/02/returns-reinvestment-opportunities-and-dividend-distribution/

construct of various pieces of UK legislation[11], that the public or consumer benefit is often expressed as a derivative of or served through other requirements, which tends to leave offences less actionable than in other countries. This should be taken into account in the statutory remit for ARGA and in any legislation.

Chapter 2 - The Expectation Gap

Q4: Do respondents consider there is an expectation gap?

The excuse of an expectation gap has been overused to hide real gaps in delivery.

I agree wholeheartedly with the conclusions of the recent BEIS select committee report on the Future of Audit concerning audit delivery gaps and their exposition in Chapters 2 and 3. These are in accord with my own previous submissions and evidence to the Kingman independent inquiry. The role that has been played by IFRS, the capture of standards and the regulator and behaving as if standards are above the law is inescapable even though individuals are in general attempting to behave with integrity.

I reproduce below part of the summary to my Kingman inquiry submission which makes points that have since been made by the BEIS select committee report and the CMA. It is recognised that the Kingman recommendations now address the Regulator issues but they do not correct the embedded consequences on standards of the acknowledged capture.

Extract from my submission summary to the Kingman Independent review of the FRC

'Company law and accounting standards

The FRC has a track record of pushing for company law to follow accounting standards. There are times where this has seemed to result in a disdain for the law. This is a cultural issue that is within the inquiry remit.

That the FRC was knowingly in the vanguard of making changes that conflicted with company law (in particular the net assets test) can be seen in an FRC letter of 8 April 2005 commenting on EU directive proposals. It is clear from the letter that the FRC is on the side of wanting company law to follow standards, not vice versa. It states:

'***Current restrictions on distributions create a rigid link between the amount that may legally be distributed and a company's statutory accounts. This creates an unnecessary obstacle to the development of financial reporting . . .'***

'In short, the Board is firmly of the view that outmoded and costly company law rules must swiftly be brought up to date'.

[11] Baroness Bowles Hansard 8 May 2019

The EU Directives did not, however, drop the requirement. In the UK, a similar requirement was in the Companies Act 1985 and became section 831 of the Companies Act 2006.
This standards issue was also 'live' in the UK where the FRC lobbied for UK company law to follow accounting standards. In part, they achieved this in the original wording of the Companies Act 2006, which allowed directors to sign off 'true and fair according to accounting standards'.

This was noticed by the investor firms (Hermes and Morley) which drew it to the attention of several ministers (there was some reshuffling at the time). There was great resistance from DTI/BIS officials and the FRC, but the Government brought in changes in 2008 that removed the sentence. This was in recognition of the fact that company law requires a different assessment than accounting standards.
Nevertheless 'true and fair according to accounting standards' remains the FRC mantra for signing accounts'

It is also worth observing that the BEIS Committee comments in their paragraph 75 about the FRC spending the best part of a decade fighting the concerns about flaws in IFRS and ICAEW's interpretation of the law. It mentions the' battle of Opinions'[12] between QCs and says it is 'surprising that four conflicting opinions did not trigger a deeper investigation by the Government and FRC'.

Again in my Kingman submission I collated evidence from FOIs and elsewhere that suggested there was, in effect, capture in the department too. Below are further extracts:

'the FRC has been far from timid in defending itself and own interests; for example, the 'true and fair' issue with LAPFF where, in collusion with officials at BEIS, FOI disclosures[13] relating to that matter [10 July 2013, FOI page 10] show an operation seemingly mounted to canvass support for the FRC view. A BIS official stated, concerning a joint commissioning of the Moore Opinion: *'[T]his is not enough on its own: we need to be thinking how to engage with, and hopefully convince, as many of the investors as possible'.*

This is a revealing statement that is made before the opinion has been obtained.

8.6 Then, after a **draft** opinion has been obtained, a statement from Richard Fleck of the FRC to BIS reads: '*We have now developed the Martin Moore Opinion to an advanced stage and I thought it would be useful to share it with you to see whether you would like to discuss any points or seek the inclusion of any points'.*19 September 2013 page 30

8.7 Given that I found this consultation and collaboration on an Opinion a little strange, I submitted a PQ asking to see the Instructions to Counsel. I was told in the reply that they are confidential and that, despite the obvious involvement of BIS from the FOI emails, the Government did not ask to

[12] BEIS select Committee Report reference 156 on page 26
[13] BIS FOI 2016/15803 page 10

see the instructions. I found the nature of this confidentiality curious: apparently, the public is allowed to see the answer from Martin Moore QC, but not the questions he was asked to address. 8.8 Then, when the opinion is finished, we can see in the same FOI on 2 October 2014, page 14 an official from the FRC asking BIS: *'[C]an you get on to your oppos at the ABI and IMA this afternoon please to drum up some support. And as they will be asked, can you brief the Big 4, the ICAEW, 100 group and the IASB. We may want investor comments more, but let's ensure we get the profession and corporates on our side'.'*

The issue of IFRS was pursued in the House of Lords Economic affairs committee in 2016[14], including in evidence by the then Deputy Governor Paul Tucker, and has been followed up extensively by myself in PQs and on the floor of the House. Clarity has been provided concerning true and fair but it is still dealt with at best reluctantly. Furthermore regulators such as the PRA and FCA also use the IFRS produced numbers for supervision and capital provisions.

The BEIS select committee urges engagement with international counterpart setters regarding IFRS. I have some experience in doing that while I was chair of the Economic and Monetary Affairs Committee in the European Parliament. It is worth commenting that IFRS is seen as a British accountancy firm sponsored construct in which the UK Government became vocal in support. When voices from the UK have since raised concerns the response is 'well it's in your own hands because you did not have to do IFRS at the company level'. That is important to realise, we can do the needed company level change ourselves, we don't need help or to await an international negotiation and group IFRS accounts continue unchanged.

Q5: If so, how would respondents characterize that gap?

Points have been made already regarding the role of standards.

Additionally, insofar as there is an actual expectation gap, there are a few things that may be confusing for the non-expert.

It is confusing – or more likely unknown - that auditors have different levels of responsibility for different parts of the annual report. Some very important features of the annual report such as key performance indicators, the viability of the entity, quality of internal controls and directors' reports do not have any assurances attached[15], may only have a 'read' requirement or a check that they are prepared in accordance with legal requirements, which in some instance may only be that they are there not of the content. It may come as a surprise to many that 'true and fair' only applies to the financial statements and nothing else.

[14] Lords EAC 16 November 2010
[15] ICAEW What auditors do: the scope of audit and Financial reporting: who does what

However it also seems that the profession makes too light of some of the provisions of s495 of the companies act. A great deal of attention is given to 'the financial reporting framework', why should any less be given to the 'requirements of the Act'?

Thus the gap is mainly one of delivery.

There will be some who have expectation that audit is a guarantee, which is unattainable, but there is well founded concern at lack of any warning about collapses that in subsequent analysis are shown not to be a result of new and unexpected circumstances. Annual accounts are wrapped up and presented quickly, yet relatively soon afterwards there have been surprises that it turns out should not have been surprises. Furthermore the FRC AQRs show what in any other field might be considered a systemic failure.

Q6. Is there also a significant 'delivery' or 'quality' gap between auditors' existing responsibilities in law and auditing standards, and how those responsibilities are currently met?

There is a gap due to focus on compliance with accounting standards as the determinant which feeds into concerns about lack of scepticism, judgement and inadequate presentation for the ordinary investor.

If the ordinary investor is not an expert in accounting standards and understanding the content of goodwill, or how standards move figures backwards or forwards in time, then they do not have a proper sense of the business conducted over the year and it is hard to see how that results in a fair view from the perspective of the ordinary investor. Some of this could be addressed by additional presentations, such as has been suggested in the context of distributions. Other brief narrative explanations could also give a better sense of the 'pipeline' than just figures done to a standard unknown to the ordinary investor.

Many suggest that the fact of Carillion getting into difficulty was discernable for example from reading notes to the accounts or looking at goodwill. Carillion raises a host of points but I make two.

First is returning to 'who is audit for' and the judge's comment in the RBS case[16] that reporting is for the ordinary investor - for which one could substitute an ordinary member of the public who has not trained as an accountant, sat on a company board or got other specialist training. The fact that concerns were not generally picked up earlier, but could and allegedly were by expert investors (paragraph 28 of this call for views) points not to the annual report and audit doing its job but to the reporting and audit not fulfilling the 'ordinary investor' criterion.

[16] *http://www.bailii.org/ew/cases/EWHC/Ch/2015/3433.html* see paragraph 54

Chapter 3 - Audit and Wider Assurance

Q7: What should be the role of audit within wider assurance?

There is some desire among the public for wider assurance, but as mentioned earlier the whole report is only just starting to be looked at by the FRC. This was an issue I raised in response to the green paper on corporate governance. It may be the case that it is too little and certainly too late so that specific independent assurance is needed.

Many of the new requirements in annual reports relate to ESG and there is no need for them to be done by auditors, especially where auditors themselves would have to have recourse to outside experts. Likewise the advent of technology for data analytics and fraud detection opens prospects that some checks could be separated out from the statutory audit.

At this stage it is hard to see whether any new assurances would simply stand alone in the longer term or whether statutory audit itself will fit within a wider assurance framework rather than assurance being absorbed into audit. In the interests of competition it is important that everything does not get swept up into statutory audit and under the same tendering process. It would also be a very strange thing to reward audit deficiency with giving auditors more work and more monopoly.

Q8: Can the level of assurance that an audit provides legitimately vary in different circumstances, for example depending on the business sector in question, and the nature of the entity's business risks?

Auditors can and do already adopt a risk based approach, both in what to concentrate upon in the audit and materiality, where it is noted it has been formalised to size and turnover rather than an absolute amount meaning that some very large sums for huge companies can be deemed 'not material' (which in itself is deserving of more attention). In many respects small and simple companies are far more thoroughly audited than large ones.

Some companies might be deserving of 'super audit' if they are very large, complex and systemic rather than there being any scaling down, but in my view this should already happen as a consequence of risk assessment.

Q9. Are the existing boundaries between internal and external audit clear?

No specific comment. The boundary should be clear.

Q10. To what extent should external auditors be able to use evidence obtained from work performed by internal auditors in drawing conclusions?

External auditors should be able to use internal audit information but not rely upon it without justification. Testing internal audit should be an important part of testing internal controls. It is noted that one of the failings reported is for auditors to rely too much on the controls of the company, assuming that large and important companies are doing a good job. This is a finding that has also been highlighted by the PCAOB. Whether earned recognition has a place (as it does for the regulator under the regulator's code) may be worth consideration but it cannot mean never checking again.

Q11. Do current eligibility requirements for external auditors focus too much on independence at the potential expense of market innovation and the quality of the audit product?

Independence is a very important criterion – essential to give an independent assurance. It is also noted that many of the criticisms laid against the tender process in the CMA report relate to overly close relationships and auditors being chosen for their 'cultural match'. Such concerns show more reason to reinforce rather than relax independence requirements.

It is hard to understand why being less independent would aid genuine market innovation. This has been stated as a mantra in many industry-originating reports but I have not seen it justified. There are more public concerns about aggressive measures of accounting or of tax avoidance being less challenged if there is overlap of audit and advisory services that have a different culture and objectives. There has also been a lot of 'innovation' in standards that has driven audit away from its roots.

Creating more competition with a wider set of organisations that can be involved in the assurance processes is far more likely to develop more choice and innovation than being able to avoid audit and partner rotation or have audit and non-audit work performed by the same organisation.

The scope and purpose of audit – Risk and Internal Controls

Q12: Should directors make a more explicit statement in respect of risk management and internal controls? If so, should such a statement be subject to audit?

It is necessary to analyse what statements should be made and why. Is the statement for the purpose of pinning liability or for greater elaboration about compliance with a statutory requirement?

Annual reports and audit reports are full of recitations that quote the law or other requirements and state that they have been done. The reader is tired by the time they have gone through the 'text book' bit and before getting to any real information. I am in favour of ongoing work that the FRC is doing to try and address the uncluttering of reports from lists of boilerplate statements, possibly putting them together in a statutory statements annex.

It is right to place responsibility on directors (especially executive directors) for having internal controls, whether stated or not, and it should be a strong requirement for controls to be audited and tested with a sceptical eye. Given that auditors are required to check the records are accurate this must surely include checking and using the controls and their output. These checks, done properly, also put them in a better position to test the controls for problems and against norms than non-executive directors. Strengthening the requirements to make sure that controls are checked is as important as a 'liability' statement.

Q13: Should auditors' responsibilities regarding assessing the effectiveness of an entity's system of internal control be extended or clarified?

If they have to give a view to the audit committee and are essentially dealing with the controls in the checks, this looks a bit like another gap. So it should be clarified beyond doubt that checking is required. As said in Q12 (and implicit in Q14 below) auditors are often in a better position to assess controls during their work than non-executive directors are so this is also good for the company. If the controls are poor and they have not been assessed, then how good can the audit be?

Q14: Auditors are currently required to report to audit committees their views on the effectiveness of relevant internal controls for listed and other relevant entities. Should auditors be required to report publicly these views?

Yes. Auditors are required to state whether accounting records are not adequate under s498. It is hard to see how they can be adequate if the controls are not, so they go together.

<u>The scope and purpose of audit – Going Concern</u>

Q15: Is the current regulatory framework relating to going concern fit for purpose (including company law and accounting standards)?

The statutory framework itself does not appear inadequate so much as that reporting to it is both boiler-plate and based on IFRS rather than company law and the company law test can be stiffer.

The proposal by the FRC to add emphasis, require robust challenge and the new auditor reporting requirement attempting to draw out comment of substance looks potentially helpful, providing more than 'yes we checked'. Checking beyond IFRS should be one of them.

Q16: Should there be greater transparency regarding identified "events or conditions that may cast significant doubt on the entity's ability to continue as a going concern"?

Sections of annual reports detailing risks can be hard to fathom with more becoming worse than less, as I once put it 'including that the sun might not shine', so that working out the more significant risks can be difficult. There may be specific events for which information can be given and when it can, it should be given unless there would be significant commercial jeopardy. In that case the fact there is a circumstance should still be disclosed and quantified as far as possible.

The scope and purpose of audit – viability

Q17: Should directors make a statement about the sustainability of the entity's business model beyond that already provided in the viability statement?

The business model should be tested on a range of horizons and review periods relevant to their business, not just copying some perceived norm, and for varying economic conditions, explaining why those have been chosen.

Q18: Should such a statement be subject to assurance?

This is a business matter but auditors may have to state if assumptions are dubious or inconsistent where it relates to financial matters.

Q19: Who might be capable of giving such assurance?

Auditors or other types of approved or specialised persons depending on the matter.

The scope and purpose of audit – unaudited information

Q20. Is there a case for a more forward-looking audit? What would be the main benefits and risks?

A main part of forward-looking in accounts is in the in-built company law prudence or safeguarding in going concern and net assets test/capital maintenance and an audit done to company law requirements would pick that up. Prudence in company law uses asymmetry, that is not recognising unrealised assets but taking account of unrealised or potential losses and is safeguarding for the future. It is important to keep that safeguarding, do it better than now and not pretend that it is possible to see the future and do away with safeguarding on the basis of forecasting things (especially profits) that are yet to happen. The clash with standards here is significant and recently reaffirmed because in the latest IFRS concept 'prudence' is defined as symmetry, aka neutrality, which rules out asymmetric safeguarding. So it does not follow company law. Proper audit should pick up any 'big bath' provisions: there was no need to throw out prudence with the bathwater.

Audit should give noticeable warnings when they are in the figures to be found, Carillion's goodwill may be an example, or the business model. Most of the forward-looking or warning that is desired may well come from an improvement in audit quality, narrative, explanations accessible to ordinary investors and the public and figures based on the company law requirements (however that is done).

Q21: Would audit or assurance over financial and non-financial information outside the annual financial statements (for example KPIs or non-financial metrics, payment practices or half-yearly reports) enhance its reliability and therefore be of benefit to users?

Yes as previously mentioned. As investing strategies and public concerns have become more widespread, such as for ESG issues, it is important for there to be some verification for qualitative matters. This could be by other organisations than auditors so as not to confuse audit and assurance and also so as not to extend the statutory monopoly.

It is justified to take such action because while there have been statements of intent in annual reports concerning matters such as diversity and payment practices, big changes and the topic appearing on board agendas as a routine only seems to happen when reporting requirements are introduced. Cross checking of the appropriateness and actual use of KPIs, rather than them being merely presentational, and the calculation methods through audit or assurance would be beneficial to building trust and understanding.

Q22. If so, what information might usefully be subject to audit or another form of assurance and why?

Directors duties under S 172 and s 172 statements, so picking up long term survival of the company, stakeholders, environment, employees and the strategy report, KPIs and all reporting done under statute and governance codes. The BEIS select committee has recommended that the whole annual report should be audited. I agree with assurance, but separate from audit, this should not all come under the statutory audit monopoly and oligopoly.

There are several advantages: reassurance for the public and the rebuilding of trust and potential benefit from discussions about the assurances such as alternative or better ways of measuring.

Audit Product and Quality - Overview

Q23: Do respondents agree that the value and quality of the audit product should be considered separately from the effectiveness of the audit process?

In principle possibly, but I am not certain that the two sides are independent.

Q24. Do respondents consider that emphasis placed by auditors on 'completing the audit file' for subsequent FRC inspection can eclipse the desired focus on matters requiring the exercise of considered judgment?

I have been told, in response questions on this and when inquiring about the culture of long working hours, that the long hours result from the pressure to finish the audit, even though audit is an ongoing matter. By extension one gets to hurried judgements. This is something that should be sorted out by auditors in their work planning as they have milestones and known dates. It is not an excuse for not exercising judgement nor failing to challenge.

When it comes to the audit file I have also been told that the energies of the FRC inspection goes into making sure every judgement is recorded rather than what the judgement has been. Unless it is quicker and public, AQR loses a lot of what could be added value. It might be beneficial to have real time AQRs done by way of observing the audit, including using independent experts alongside regulator staff. Attending the meetings between company and auditor would be an important part.

Audit Product and Quality – Binary nature of audit & Producer-led

Q25. What additional benefit might a switch from a binary audit opinion to a more graduated disclosure of auditor conclusions provide?

This sounds interesting but needs careful thought on how it is implemented. Benefits might be that it draws out more information about judgement, give strengths and weaknesses more clearly and an indication of something between 'material' and 'no comment' on the cumulative effect of concerns. It may also give insight into culture, especially when it comes to looking at successive audits.

It might be problematic if a good grade were to become regarded as a guarantee or if it leads to even more resistance to qualification by the auditor and in essence never a 'fail' just a lower grade. It might be useful to have a few key targets such as controls and the aggressiveness of accounting.

The cumulative effect of every 'micro-judgement' being systematically up against the aggressive edge rather than a spread of greater and lesser aggressiveness is significant, therefore recording and reporting on the aggressiveness and how material that is to the accounts would be useful. This is especially the case when the ICAEW says[17] that the dividing line between aggressive accounting and fraudulent financial reporting is rarely clear. It is up to auditors to make it clear and to measure and report on systematic aggressive accounting, including for reasons of culture. In the end that is also fairer in company to company comparisons and a valuable warning or assurance. Aggressive accounting should be regarded as drug best not touched for fear of overdose, so the auditors need to expose addiction.

Q26. Could further narrative be disclosed alongside the opinion to provide more informative insights?

Important things should be stated as they are found, there should be care not to gloss. Auditors should be steered away from feeling that the safe option is to say the minimum, whether for fear of litigation or otherwise. The presumption and burden of liability should act in favour of speaking up rather than in favour of silence.

Q27. What would prevent such disclosures becoming boiler plated?

Boilerplate statements without reasoning could be discounted in the assessment of whether the responsibility to comment has been discharged. This is part of changing the balance of liability in favour of disclosure mentioned in other questions later.

Q28: To what extent, if any, has producer-led audit (including standards-setting) inhibited innovation and development for the benefit of users?

Producer-led audit and producer-led standards are two sides of the same coin, and linked together have trapped audit into the ‘correct by process and standards’ approach that in turn has blunted scepticism and use of judgement. Of course there is attractiveness for the producer to have more certainty over compliance but it does stifle innovation because of the aversion to risk and making judgements.

There is a pervading notion that any kind of statement beyond the anodyne is in some way ‘qualifying’ and something to be nervous about with regard to liability. Whether this is the genuine reason or an excuse to avoid making judgements or both is open to speculation. Markets are more robust to disclosures required by the SEC in the US and there is no reason why the UK market would not be similarly robust.

If it is companies who are forcing auditors into the ‘defensible position’ based on standards, then companies must change tack or the question from Sir John Kingman about independent appointment of auditors may need to come into play.

[17] ICAEW Financial reporting: who does what p8

Chapter 6 - Legal Responsibilities

Q29. What role should auditors play in determining whether the directors are complying with relevant laws and regulations, including with respect to matters of capital maintenance? Is it appropriate to distinguish between matters which may materially affect the financial statements and other matters?

When I have asked big 4 auditor firms in general about the checks that they have done regarding s 495 'requirements of the Act' and s393 'have regard to the directors' duty only to approve accounts giving a true and fair view' the response has been that it is only about very limited parts of the Act and the true and fair view is tied to the IFRS prepared financial statements. I have not obtained any admissions about a company law true and fair override, which is among the reasons why I pursued its confirmation in Parliament[18].

My experience has thus been much the same as the FRC found in its thematic review in 2013 that it is not seen as an important feature. This is a delivery gap and I agree with the proposals from Sir John Kingman that the statute should mean something.

Q30. Does a perceived inconsistency between company law and accounting standards as regards distributable reserves inhibit auditors from meeting public expectations? How might greater clarity be achieved?

As explained in the introduction, Q4, and elsewhere, like the BEIS committee I researched and found that there is an <u>actual</u> not just 'perceived' inconsistency between standards and company law and it is a significant contributing part of the expectation/delivery gap. The belief that standards have primacy has led to a culture of denial among the accounting and auditing hierarchy. In addition to the 'gap' and failures this breeds dissatisfaction about the professions because company law is conceptually and instinctively much easier to grasp.

Distributable reserves are the crunch point where liability bites on companies and auditors. Collapse of a company shortly after generous distributions is seen by the public as 'robbery' of their investments, pensions and taxes that auditors are there to help prevent. It is not an answer for them to say the figures from the standards didn't show it.

The situation could be helped immediately by recognising fully that company law requirements sit as extras on top of standards and should be checked and visibly addressed. It would be helpful for there to be separate elaboration of realised and unrealised profits, assets and liabilities and any distributable amounts.

More generally a full fix would be either to return to true company law based individual accounts (not the present IFRS or IFRS look-alike UKGAAP) and only use IFRS for group

[18] HL 5280

accounts like the rest of the EU does. There might be other alternatives such as a separate and strict solvency test.

Q31. Should distributable and non-distributable reserves be required to be disclosed in the audited financial statements?

Yes as above. It may also be relevant to give some colour about the unrealised assets and liabilities and timescales for an appreciation of the in-year cash position and expectations regarding the unrealised elements. These issues are far more relevant today than in the past with the ever increasing moves to contracted services rather than outright purchase.

Q32. How do auditors discharge their obligations relating to whether the entity has kept adequate accounting records? Are the existing statutory requirements effective in setting the bar for auditors at a high enough level?

How can you check for material misstatements and fraud without forming a pretty thorough view on the state of the accounting records? It would seem to need to be integral with checks on controls. It is a statutory requirement under s498(2) to state if the accounting records are inadequate. It is not possible for me to assess how well that is done.

Chapter 7 - The Communication of Audit Findings

Q33. Should there be more open dialogue between the auditor and the users of their reports? For example, might an annual assurance meeting open to all stakeholders prove valuable?

If there are meetings then representatives of ordinary investors would need to be able to attend as well. Meetings should not lose sight of the fact that the ordinary investor is the main receiver of the audit (see Q1 and RBS case) so it would be important that 'expert users' did not skew matters by being the only attendees. Transparency over who had attended meetings would be important. A forum for general matters is more the remit of the regulator. However annual assurance meetings linked to the AGM and auditor presentations seems a good route.

Q34. Should more of the communication and resulting judgments that occur between the auditor and the audit committee be made transparent to users of the financial statements?

Yes. They should also be part of real-time AQRs.

Q35. Should there be enhancements to the extended audit report, such as an obligation to update on key audit matters featured in the previous audit report?

Yes, matters arising is a normal way for things to be followed up after meetings, so why not apply it to audit reports. It would fit usefully in with proposals for auditors to present at annual meetings and also with ideas to revise annual reports to be more focused on the things that change. However in the first instance it is for the directors to report how any matters have been addressed.

Chapter 8 - Fraud

Q36. Do you believe that users' expectations of auditors' role in fraud detection are consistent with the requirements in UK law and auditing standards? If not, should auditors be given greater responsibility to detect material fraud?

I am in agreement with the BEIS committee that there is a requirement to look for and detect fraud. It is alarming that the large audit firms did not give that view. The FRC has also stated that it is not being dealt with properly and AssetCo has set a very high legal expectation.

Speaking to auditors of small companies they do not seem to be in any doubt about being on the lookout for fraud. If you are auditing a brewery you check which barrels are full. Therefore it seems that it is the large company auditor's expectations rather than the user's expectations that are out of step with UK law and auditing standards.

Given that there appears to have been an actual abandonment of responsibility for various aspects of fraud detection covered by other questions such as Q32 about checking on keeping adequate records and also issues around internal controls, one solution may be to immediately open up fraud detection to non-audit IT firms with an appetite for this kind of detection. This may be more fruitful than leaving it in the hands of reluctant auditors who don't want to do it other than in an incidental way.

Nevertheless, even if that line were taken a requirement to report fraud found 'incidentally' and to be alert should remain. Also given the statement in the ICAEW document[19] that 'The dividing line between aggressive accounting policy and fraudulent financial reporting is rarely clear' that line must be very actively examined by auditors and disclosures made in the context of reporting on aggressive accounting, stating if a company is using it and the effect that it has including on remuneration. It is not satisfactory to leave matters as the ICAEW document says that fraud 'often only emerges over time as a situation deteriorates'. That is tantamount to saying let aggression run riot, slip into fraud and take notice when it is too late.

[19] Financial Reporting: who does what - foot of page 8

Q37. Do existing auditing standards help to engender an appropriate fraud detection mindset on the part of auditors?

It seems not at least for auditors of large companies. Bring in the competition.

Q38. Would it be possible to devise a 'reasonable person' test in assessing the auditor's work in relation to fraud detection?

Yes. Possibly a sceptical person's test.

Q39. Should auditors be required to evaluate and report on an audited entity's systems to prevent and detect fraud?

Yes unless that is separately and independently commissioned from a non-audit firm, but there are substantive requirements in statute.

Chapter 9 - Auditor Liability

Q40. Is the audit profession's willingness to embrace change constrained by their exposure to litigation?

The large audit firms cite concern over liability but they have structured themselves to be able to isolate parts of their networks in order to be resilient and they have insurance. The usual presumption would be that concern over litigation would stimulate better audit but that has not happened. The industry response seems to be to have changed the way the law is to be interpreted to suit them, through collective assertion.

I am not against changes to liability in principle because the original effects of unlimited liability meaning facing ruin is much diluted once firms are large with many partners and high levels of insurance. It probably bears down more heavily on smaller firms. However, for the reasons given in the call for views, substantive change is difficult and it is also the wrong message for the present time, it would look like rewarding failure.

With regard to more disclosure it might be possible to help a change of attitude if it is made clear, in law, that as more transparency and disclosures are required from auditors the legal balance is in favour of making disclosure rather than silence for fear of reprisals and allegations of drawing conclusions for which there is no reasonable basis.

Q41. If there were a quantifiable limit on auditor liability, how might this lead to improvements in audit quality and/or effectiveness?

I do not know how it might improve quality or effectiveness to be less scared of not being diligent. It would make it even more likely that cases were always settled and never go to court, which prevents the development and interpretation of law. AssetCo is seen as stunning because a case going the distance is rare and meanwhile practice has drifted away from statutory intent.

Q42. Should company law make auditors potentially liable, or otherwise accountable, to all stakeholders who reasonably rely on their audit work and their published auditor's report?

Yes. Action in the public interest should also be possible and it is important that regulators should not be litigation shy or outgunned.

Q43. How might quality of the audit product be improved if the approach to liability was altered, and what reform might enable the most favourable quality improvements?

This is mainly as answered above, modify the law to enable more disclosures without fear of challenge that it has no reasonable basis. However there should be no lifting or lightening of checking and reporting responsibilities , these should be stringently applied according to law.

Q44. To what extent (if any) are firms unable to obtain the desired level of professional indemnity insurance to minimise the risk of being unable to meet a significant claim relating to their statutory audit work? How significant is this risk for both the largest firms and other firms undertaking audits of Public Interest Entities?

Don't know. This is not an area that is usually transparent.

Chapter 10 - Other Issues - Technology

Q45. How far is new technology actually used in audits today? Does the use of technology enable a higher level of assurance to be given?

Most is still under development. It should be used and be capable of being independently provided and tendered for by non-auditors. The regulators should be increasingly engaged in having technology too.

Q46. In what way does new technology enable assurance to be given on a broader range of issues than is covered by the traditional audit?

Agree with the points made in the call for views document. AI for reading and comparison with former years of the whole document is an obvious example and one that it would be good for regulators to have access to. No examples to input.

Other Issues - Proportionality

Q47. Are there aspects of current audit procedures or output that are no longer necessary or desirable?

Anecdotally I am told that detailed recording or micro-judgements has a crowding out effect.

Q48. Given that a zero failure regime is not attainable (and arguably not desirable) how should the Review calibrate the value of audit in relation to the limitation of potential failure?

At the heart of reform is public confidence in business and in audit, so it's not a viable option to just carry on the same. As Sir John Kingman explained to the BEIS committee, it is analogous to the upgrading of financial supervision after the crisis. It is not an 'if it ain't broke don't fix it scenario'. However a lot of the fixing is to return to basics.

Q49. Does today's audit provide value for money?

Given that there are other services that are more expensive and there are suspicions that it has also sometimes been a loss leader then the answer is yes. However in terms of whether audits are of sufficient quality, is it keeping business sufficiently honest or helping to impact culture, the answer seems, rather too many times, to be no.
Although audit is meant to be sceptical and this inquiry is looking at shortcomings, it is worth noting that audit committee chairs in evidence to the CMA said that changing auditor was generally a positive experience. In my own limited experience of tendering and appointing new auditors in three organisations that is true: new viewpoints, new eyes and new ideas have been helpful. There should be a positive side to audit for the business as well as for the public.

Q50. How should the cumulative costs of any extension of audit (whether stemming from this Review or other drivers of change) be balanced against the likely benefits to users?

In the benefit analysis the public interest is key and it is hard to put a price on trust in the present environment where so much of society feels alienated. Reversal of the decline in confidence in business, not just in audit, is at stake. Like the new regulators and legislation after the financial crisis, much of this is not an option.

Better business should also be of benefit to companies, therefore the measure cannot be one of simply what is the percentage increase in cost to the company. It should also be taken into account that a lot of what is sought is not an extension to audit, but doing audit as it was intended.

Other Issues - Shareholders

Q51. What use do shareholders currently make of audit reports? Are they read by shareholders generally? What role does AI play in reading and analysing such reports?

Different types of shareholders read different parts of annual reports. Others, and the general public/end beneficiaries will read what is commented on in the press or other media. AI should help in analysis of reports, including year to year comparisons and for internal consistency. It may well have wider effect beyond that of auditors and analysts.

Q52. Would interaction between shareholders and auditors outside the AGM be practical and/or desirable?

I think this is difficult. Factions of shareholders should not be able to apply the wrong kind of pressure. Transparency would be important. The first port of call should be the audit committee.

Q53. How could shareholders express to auditors their ex ante anxieties to help shape the audit plan? Should shareholders approve planning matters for each audit, including scope and materiality?

Approval of materiality should be put to shareholders at the AGM and so could the outline of scope and maybe the directors could call for specific areas of interest. The discussion could be an adjunct to the auditor approval process and to any presentation by the auditor at the AGM if those ideas are taken up.

Q54. What assurance do shareholders currently obtain other than from audit reports?

None for an ordinary shareholder other than information that may come from NGOs or proxy advisors but those are advice rather than assurance.

Other Issues – Culture

Q55. In what way would it be possible for auditors to report on the culture of the entity whose financial statements are being audited?

Auditors could do financial culture such as aggressiveness of accounting, its effect on bonuses and performance are obvious ones. It is important not to overload statutory audit. Things to do with culture would be better assured by bodies more expert in culture.

Q56. How can auditors demonstrate that appropriate scepticism has been exercised in reaching the judgments underlying the audit report?

Over time audits should improve and speak for themselves. AQRs should improve and the regulator and independent experts doing real time observation should be part of AQR. Within an audit more transparency over judgements could be given so everyone gets to understand what they are talking about.

Q57. Should the basis of individual auditors' remuneration be made available to shareholders?

Yes.

Other Issues - Cost

Q58. Do respondents view audit costs as generally too high, about right or insufficient?

As far as I know they are probably about right, if anything cost should maybe be higher in return for more focus on scepticism and judgement and delivering a better audit. Cost has not seemed to be the determining issue according to the CMA interviews with audit chairs.

Q59. Would users of financial statements wish more detail on the make-up of audit fees?

Yes because it gives insight into the relative importance of where the money is used and also how much is being outsourced and a view taken on how controlled that is. This is also useful for the regulator.

Q60. Is the profitability of the audit function sufficient to sustain a high-quality audit industry?

Yes, however if not prices will rise. It seems as if the audit quality and gap issues are not due to cost but rather to do with audit having been skewed away from statute. The fact that the call for views paragraph 86 even asks a question phrased 'whether there is support for the primacy of law' is telling in terms of where matters are.

Independent Review of the Financial Reporting Council

Response by Sharon Bowles (Baroness Bowles of Berkhamsted)

Declaration of interests. I hold company directorships which are included in the House of Lords Register of interests

This is a personal response based on my substantial policy and legislative involvement in company law and International Financial Reporting Standards (IFRS), including as an MEP from 2005 to 2014, serving on both the Legal Affairs Committee and Economic and Monetary Affairs Committee and chairing the latter from 2009 to 2014. Since then, I have researched company law for my own interest and legislative purposes, including responding to other calls for evidence on corporate governance and corporate liability.

Context and executive summary

The Financial Reporting Council (FRC) has been under fire over the last few years for its inadequate oversight of corporate governance, failure to investigate the audits of banks that collapsed in the Financial Crisis, as well as for letting off KPMG for its audit of HBOS and a list of other high-profile failures including Co-Op Bank, Tesco, BHS and Carillion. Moreover, its shortcomings have been exposed in responses to the BEIS Select Committee Inquiry into application of s172 of the Companies Act 2006, the Government's Green Paper on Corporate Governance and the recent joint Select Committee Inquiry into Carillion.

As has happened before, when criticism gets to serious levels, the FRC responds by defending itself and making limited reforms that are long overdue. Although this might be welcome, underlying both its failures and its reactive responses is the issue of culture. I believe this stems directly from its current structure.

Denial of public-body status

Since 2004, the FRC has been set up as a 'market led' collaboration two-thirds funded by a voluntary levy on industry. It has aggressively maintained that it needs to be a private body in order to keep this 'collaboration' going and has gone to extraordinary lengths for over a decade and a half in pursuit of that objective. In 2004, it baffled the Cabinet Office[1]. The FRC makes its case in a letter[2] which states:

- 'The business, investor and professional communities *contribute* *<u>at the most senior levels</u>* *to the* *<u>development of our strategy, the determination of our priorities and the monitoring and evaluation of our work</u>*'

[1] ONS FOI 2017/3410 doc 16
[2] ONS FOI 2017/3410 doc 42

- '*They contribute [via voluntary payments] because they believe they can have a meaningful impact on our work*'

- '*Designation would change our collaborative relationships*'

- '*It would give pre-eminence to government a one third contributor to the FRC's core costs'*

- '*It would establish a degree of accountability to the Government which would alter in an adverse way our relationships with the business'*

- *'Copying this letter to the President of the CBI, and the Consultative Committee of Accountancy Bodies' who represent the other funders'*

All-in-all, it is a comprehensive list of what defines a captive regulator. Such comments are unacceptable coming from a regulator that, by function, must have at its heart protection of the public interest – not the interests of those it regulates.

What is perhaps surprising is that both HM Treasury (HMT) and the Department for Business, Energy and Industrial Strategy (BEIS) have stood firmly behind this view and gone to quite extraordinary lengths to try and persuade the Office for National Statistics (ONS) to reclassify the FRC from public-body, which it was from its inception in 1990, to private status[3].

It is beyond extraordinary that even on its website the FRC's strategy statement for 2018/21[4] has a section headed 'The future for the FRC', which reads:

'*We aim to meet the highest standards of governance and accountability as a public body, operating within the framework agreed with the Government and independent from those we regulate. Our precise classification as a public body is still under consideration by the Government'***.**

This is the first acknowledgement that it will at last act like a public body. However, the FRC was classified as a public-sector body, and always was so, in 2004. The ONS reviewed and reconfirmed that status in 2007, 2010, 2011, and yet again in 2014[5] – adding that it was public by function as well as governance. Nothing is unclear other than that the FRC has resisted behaving as a public body and persists in doing so. The answer to my PQ HL 8896[6] confirms that it held public-body status in 2004. This was never revoked, although both the FRC and the DTI/BIS acted as if it had been suspended.

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3 ONS FOI/2017/3410 all documents see especially doc 59
4 FRC Strategy 2018/21 foot of page 8
5 ONS FOI document 59 see background in final NACC consultation
6 HL 8896

The answer to my PQ HL4991[7] confirmed the 2014 classification and that BEIS was continuing to examine whether there was scope for further review. It also stated that the 'BEIS strategy' concluded in 2017 that they should work with the FRC on the application of all relevant [public body] guidelines. It states: '*Until that point, the FRC determined its own policies on these matters*'**.** The reply also states that: **'***Decisions on the application of the guidelines, during the prolonged period in which the status of the FRC as a public body was the subject of or pending review, were taken by departmental officials under the delegated authority of the responsible departmental accounting officer***.'**

It would appear that officials in BEIS have bypassed Ministers to allow the FRC to disapply relevant guidelines. My PQ HL 7591[8] confirms that this extends to the managing of public money requirements on matters such as procurement and (see HL9366[9]) salaries.

This also demonstrates an astounding lack of awareness and an absence of appropriate culture on the part of a regulator that is in charge of making companies behave properly.

Returning to the FRC strategy statement, there is also a reference to 'operating within the framework agreed by the Government'. This is presumably a reference *inter alia* to the arrangement by way of a memorandum[10] and the permissions by officials that allowed the FRC to waive public-body guidelines so as to avoid the requirement to act like a public body on a range of matters from salaries to FOI to procurement. The memorandum was severely deficient from the outset, made in expectation that public-body status would be removed[11], is not legally binding, describes many responsibilities as voluntary and was never updated, replaced by a statute (although Patricia Hewitt mentioned that possibility) nor scrutinised by Parliament.

Presumably this memorandum is at least since 2010 somehow the basis for officials rather than ministers running the FRC policy at BEIS and its predecessors. This appears particularly unfortunate given the role of Stephen Haddrill at the DTI in setting up the FRC to his current role at the FRC where he is overseen by his wife who is a senior civil servant at BEIS. There are other FRC-related guiding hands that seem to have been active for decades too and which have only just stood down with the announcement of this inquiry.

The outcome is that although having been given public body status in 2004, and in effect since inception, the murky arrangements for the FRC's operations have been condoned by officials who have allowed the FRC to repudiate the requirements of their status.

[7] HL 4991
[8] HL 7591
[9] HL9366
[10] MoU between FRC and BIS July 2010
[11] HL 4990

Measured against the yardstick of standards in public life, it is hard to see how the FRC has lived up to that expectation.

Additionally, the response to PQ HL6436[12] states: '*The FRC is the prescribed body in company law to issue UK accounting standards. The members of FRC Board are <u>not required to be designated to represent the interest of public investors in order to set accounting standards</u> so no assessment of this is necessary*.'

This is clearly something that needs fixing.

<u>Company law and accounting standards</u>

The FRC has a track record of pushing for company law to follow accounting standards. There are times where this has seemed to result in a disdain for the law. This is a cultural issue that is within the inquiry remit.

That the FRC was knowingly in the vanguard of making changes that conflicted with company law (in particular the net assets test) can be seen in an FRC letter of 8 April 2005[13] commenting on EU directive proposals. It is clear from the letter that the FRC is on the side of wanting company law to follow standards, not vice versa. It states:

'Current restrictions on distributions create a rigid link between the amount that may legally be distributed and a company's statutory accounts. This creates an unnecessary obstacle to the development of financial reporting . . .'

'In short, the Board is firmly of the view that outmoded and costly company law rules must swiftly be brought up to date'.

The EU Directives did not, however, drop the requirement. In the UK, a similar requirement was in the Companies Act 1985 and became section 831 of the Companies Act 2006.

This standards issue was also 'live' in the UK where the FRC lobbied for UK company law to follow accounting standards. In part, they achieved this in the original wording of the Companies Act 2006, which allowed directors to sign off 'true and fair according to accounting standards'.

This was noticed by the investor firms (Hermes and Morley) which drew it to the attention of several ministers (there was some reshuffling at the time). There was great resistance from DTI/BIS officials and the FRC, but the Government brought in changes in 2008 that removed the sentence. This was in recognition of the fact that company law requires a different assessment than accounting standards.

12 HL 6436

13 FRC letter 8 April 2005

Nevertheless, 'true and fair according to accounting standards' has remained the FRC mantra for signing off accounts.

The inquiry is not set up to investigate the true and fair issue, although it is worth noting that the response to my PQ HL5280[14] does settle the issue by acknowledging that there is a true and fair override. **What concerns this inquiry is that the conduct of the FRC points to a regulator more concerned with pursuit of its own policy objectives, and defending them, than recognising the law[15],** and which at times does not seem to know what was or was not the law[16].

Conclusion

As is usual whenever there are complaints about the FRC, they propose mechanisms to make themselves better. The changes inevitably become much diluted once they get into the 'collaborative consultation' process, and always the promise to reform distracts from fixing the fundamental flaw.

The FRC can only be fixed by root and branch reform that creates a statutory and truly independent regulator that cuts out all the links and individuals that have supported such a flawed and culturally oblivious set up. It is hard to see how a continuing, even if reformed, FRC can make the necessary break with the past.

Responses to questions

FRC purpose and function

Q1: What should the FRC's objective(s) be? Is its present mission statement the right one?

Summary: The FRC, or its successor, needs a more compelling mission centred on enforcement and which includes a direct duty of care to the public interest.

The FRC/New Regulator must be set up by full statute for all its activities. The statute should embed the duty of care to the public interest as well as the primacy of company law over any other standard setting or guidance

1.1 The FRC's mission statement is insufficient. The use in the first sentence of the term 'promote' before transparency and integrity underscores the lenient nature of the mission. The FRC/New Regulator mission should be to enforce Company Law in full, unequivocally, and to ensure that any standards or guidance for which it has (or continues to have)

14 HL 5280
15 FRC Minutes 26 September 2013 'focus of any debate should be on the quality of such standards rather than their legality'.
16 Appearances of Stephen Haddrill before numerous Parliamentary Committees, for example House of Lords Economic Committee Q197 2010 Lord Forsyth, 22 July 2014 whole evidence session.

responsibility are fully compatible. The same should apply to all its activities, with the emphasis on enforcement and ensuring rather than promoting and encouraging.

1.2 In addition to the mission statement quoted in the call for evidence, the FRC website claims that 'The effect of our work is to ensure a strong flow of capital into the UK that is beneficial to the economy and to society as a whole'. This declaration of (hoped for and dubious) outcomes puts any benefit to society as a trickle-down derivative, not a primary function. It is also reminiscent of the FSA's competitiveness requirement and, indeed, suffers from the same flaw.

1.3 As recent events with Tesco, Co-Op, BHS and Carillion have shown (and others before them), it is the public who are on the hook for corporate failures: as savers via institutional investors, as taxpayers through pension bailouts and as stakeholders such as creditors and employees. It is, therefore, necessary for the FRC/New Regulator to owe a duty of care to the public. It is insufficient to view and supervise corporate behaviour only through the lens of investors.

1.4 It is an oft-repeated mantra, made during the 2004 company law review, that it is the Government which is responsible for the public interest, through legislation, and that it is not the place of companies to share that responsibility. Government can, of course, impose a duty of care sectorally, such as in health and safety legislation. More generally, a logical derivation follows from limited liability in that it is a 'bargain' with society, through which investors as well as companies are protected from unlimited liability. Accordingly, a duty of care is owed in return.

1.5 In any event, a consequence of the Government having that public-interest responsibility means that a similar responsibility must devolve to any regulator/supervisor who exercises power delegated by the Secretary of State. This is part of the reasoning behind why regulators are classified as public bodies by function (ESA 2010).

Q2: Does the FRC's name remain right?

Summary: No, the FRC name does not reflect the wider non-financial reporting, audit control and corporate-governance responsibilities for which the FRC/New Regulator has or should have formal responsibility.

The inclusion of the word 'Council' implies the multi-stakeholder market-led model that is no longer fit for purpose.

A change to the name would mark a change from a tainted name and regime, as was the case with the FSA.

2.1 The FRC has wider responsibility than financial reporting. It has an expanding role in non-financial reporting and corporate governance. This more holistic nature should be reflected in its name in just the same way that there is more realisation of the need for wider corporate reporting – as reflected in The Companies (Miscellaneous Reporting) Regulations 2018.

2.2 The FRC was set up as a collaboration, and the use of 'Council' in its name is now redolent of its representative nature with regard to its stakeholders. In its own words, in the FRC December 2004 letter[17], it states: '*The business, investor and professional communities contribute at the most senior levels to the development of our strategy, the determination of our priorities and the monitoring and evaluation of our work'.*

2.3 This collaboration is still present and there is surprise in some quarters when the FRC departs from the consensus. This is highlighted, for example, in an April 2018 article by the ICAEW[18] on audit quality and a possible separation of accounting and audit. The introduction states: '*But when **even** the FRC breaks that consensus*', while the EY contribution notes that *'[W]e share across the professions with the ICAEW and the FRC, so it is quite a collaborative environment'*.

2.4 A name change alone will bring neither culture change nor compensate for the lack of a proper statutory basis, but it can help mark a package of changes.

Q3: Are the functions and structure of the FRC still relevant and appropriate, or is there a case for any structural change? Should any of the FRC's functions move to other regulators?

Summary:-
- Structure and distribution of functions must ensure audit can properly challenge, including standards.
- Create a proper statutory Companies Regulator
- Remove accounting standard setting to an independent body
- Transfer audit discipline to Insolvency Service
- Possibly merge with Insolvency Service and Companies House
- Less reliance on accountancy/audit professions and related law firms

3.1 Current structure. The current structure is no longer relevant. Indeed, since the 2004 revamp, the FRC was undermined, rather than rising to new challenges. The FRC followed what was essentially a trade association model that has deeply influenced culture and led to a captured regulator by definition – see, again, the FRC's own December 2004 letter where it is described as a collaboration. It is inappropriate for a regulator to be so intimately entwined with the professions and companies that it regulates.

3.2 New structure and functions The FRC/New Regulator should be set up by a proper statute with all necessary powers and duties, including the duty of care for the public

17 FRC December 2004 letter, same as in the introduction
18 April 2018 article icaew

interest that derives from Government delegation of power. The combination of structure and functions must be such as to ensure they do not mark their own homework.

3.3 The FRC/New Regulator should not be responsible for both accounting standards and auditing standards. In particular, in combination with IFRS, this creates a toxic feedback loop that has taken the judgement out of auditing and made it more of a tick-box exercise that is premised on accounting standards and which has been called 'righteous by process'. This has led to a bias away from the public interest and towards making life for auditors easier and safer, although it still leaves (possibly unrealised) the separate check for true and fair and compliance with company law in the hands of directors.

3.4 There has been continuing FRC formal guidance to the effect that an appropriate directors' statement is 'true and fair according to IFRS'. This has served to reinforce the 'righteous by process' approach even after that provision was removed from the Companies Act 2006 at the insistence of Parliament and in the face of campaigning by the FRC. Indeed, the FRC has now acknowledged that there always was a true and fair 'override' for 'special circumstances'; nevertheless, they have been at the centre of an approach that has demoted the use of judgement.

3.5 Monitoring and enforcement of company law and audit are closely related and so it makes sense for the FRC/New Regulator to be responsible for audit, but not for accounting standards in order to enable criticism of standards and ensure that audit looks beyond standards, which currently does not seem to take place. For example, anyone looking beyond standards with Carillion would have recognised the debt aspects of reverse factoring.

3.6 It is also desirable to separate the audit standards from enforcement – ideally in a separate body.

3.7 It might be appropriate for the Insolvency Service to undertake auditor discipline, although some statutory changes to the insolvency service must also take place.

3.8 An alternative could be to have two independent audit standards and enforcement branches in the same regulator (as with the FCA), although some think that is not the best option there either.

3.9 Companies House could also be incorporated into any new regulator.

3.10 Too much reliance has been placed on the accountancy profession for setting both accounting and audit standards. This is also the case with the IASB. Standards should draw much more heavily on sources beyond accountants and include suitably independent academics. This must also be the case with the board and any committees within the regulator.

Q4: What lessons can be learned from other countries' regulatory systems? Which ones?

4.1 Company Law is very country-specific, which is in part why international accounting standards can conflict with it – a point well recognised in the US refusal to adopt IFRS. There is no escaping the fact that law and standards, if not in harmony, must both be catered for, something that Paul Tucker recognised in his appearance before the Lords Economic Affairs Committee on 16 November 2010[19] (referenced further under Q32). Culture as embedded in regulators and Government is also key.

4.2 US regulators seem to have been more effective, and more feared, in recent years than in the UK, although it is recognised that there are concerns globally with audit. It is notable that the US maintained separation of standards and oversight with the Financial Accounting Standards Board and the Public Company Accounting Oversight Board.

4.3 Other Commonwealth countries have built regulatory regimes that have scored more highly in international ranking of corporate governance, such as South Africa.

4.4 Similarly, Australia retained separation of accounting standards and its 'FRC' body in the way that the UK used to.

4.6 In Australia, governance at board level is much stronger due to a range of measures intended to change culture. There is, for example, more awareness of and scope to apply criminal liability. They have at least made an effort to catch all bad behaviour by permitting prosecutions for 'unconscionable behaviour'. There is also stricter application of comply or explain, and the expectation is geared more toward a good explanation. The code is also maintained by a body other than the regulator.

Q5: How effective has the FRC been in influencing wider debates that affect its ability to deliver its objectives – for example, around audit competition, or its legal powers?

5.1 The FRC does engage in consultations but it is questionable whether there has been positive influence.

5.2 As previously noted, the FRC has been part of the consensus lobby that has been effective at influencing regulation in the UK, EU and at the IASB. It is hard to separate out the FRC's policy contribution but it has been official input and used at the political level to suggest 'regulators endorsement' for what is essentially a corporate line. It was my personal experience in the European Parliament that the FRC seems only to have expounded the views of those they regulate. We witnessed lobbying against dual-auditor suggestions, audit/accounting split, break-up of the Big 4 and not a jot shorter time limit than the CMA proposals on audit rotation. Only recently, when under pressure, have they finally broken ranks.

[19] Lords EAC 16 November 2010

5.3 The FRC has been a cheerleader for things in both in IFRS and in Company Law that have caused the kind of problems that are coming to light.

5.4 The FRC backed the company law provision of 'true and fair according to standards', lobbied against Parliament removing it, and maintained it in guidelines.

5.5 The FRC was strongly in favour of moving to neutrality in IFRS[20], thought that company law was outdated, lobbied against it and then basically ignored or reinterpreted it to achieve its own objectives.

5.6 The FRC pushed through the adoption of IFRS for separate financial statements in the UK. This exceeded the EU legal requirement, which was only for group level yet in public the 'we had to do IFRS because of the EU' excuse was and still is commonly stated. Other EU countries did not make similar changes at the level of separate financial statements.

5.7 Pushing IFRS was a successful lobbying exercise, but one that has had consequences both in its neutral rather than prudent effect and also (as also explained in Q18) by limiting consideration of concerns coming from the UK about IFRS.

Q6: Is the current balance between cross-cutting reviews and firm-specific investigations most effective?

6.1 It doesn't appear that anything much has been effective, although in theory this is a reasonable combination.

6.2 There seems to be a reluctance to intervene even when things are found out. How is a decline from KPMG having 35 percent unacceptable audits allowed to grow to 50 percent before any disciplinary and audit tightening is suggested? Indeed without criticism and recent scandals, would anything have been addressed?

6.3 The investigations should be used to bring forward more intelligence about threats and new developments and to take action against those developments that, for example, flatter or conceal, whether intentional or not.

<u>Impact and Effectiveness</u>

Q7: What are the FRC's strengths and weaknesses?

7.1 Any reputational strength that the FRC had pre-dates 2004. In my personal experience in the EU, this has been noticed and the FRC is not so well regarded as the FRC would have you believe. Criticism has been made openly in hearings of the ECON committee, most notably by Angel Gurria, Secretary General of the OECD.

[20] FRC 8 April 2005 letter as before

7.2 Its weaknesses are many. They include failing to investigate audits of banks after the financial crisis, clearing the HBOS auditors, lowering the standards that auditors are measured by and applying the softer measures retrospectively, and failures on BHS and Carillion that have led to public and Parliamentary opprobrium.

7.3 Their main strengths seem to be those with bad effect – lobbying on IFRS and against getting to grips with dominance of the Big 4.

7.4 The FRC is good at making presentations, especially to defend itself, but it is an ineffective regulator. It has been prepared to push a little further when there is the 'comply or explain' get-out in the governance code, but it is not strict enough when it comes to what is needed for explanation. The 'explain' should be much closer to seeking permission for a derogation than a perfunctory statement in the annual report that something does not suit the business.

7.5 The FRC issues guidelines that can be helpful but care has to be taken that this does not create a checklist of boiler plate statements that are copied and pasted. Some guidelines and interpretation of CA2006 have been unhelpful or wrong (see also Q8)[21].

Q8: The recent joint report on Carillion from the Business, Energy and Industrial Strategy and the Work and Pensions Select Committees considered the FRC to be characterised by "feebleness and timidity" and recommended that a change of culture and outlook is needed. Do you agree? If so, please cite relevant evidence which informs your view.

8.1 I agree. The feebleness and timidity towards those it regulates and the cosy culture and outlook all stem from the 'collaborative' stakeholder-driven model which means the FRC is captured by design. That has to be driven out.

8.2 There does not seem to have been a desire to break out of the captured arrangement, indeed quite the opposite, and the FRC has come out fighting to protect it. The classification saga demonstrates this. Every time the ONS cites an aspect that makes the determination of the FRC that of a public body, the FRC sets about making the changes to board appointments and challenging the 'in perpetuity rule'[22] in an attempt to be reclassified. Yet it behaves as if public body classification had never taken place and has yet to approximate its behaviour to that expected of a public body.

8.3 PQ 4991[23] shows that the FRC was in charge of how it behaved and made the cultural choice to be far departed from public-body behaviour. As I have already stated, waiving the application of public classification guidelines while the classification of the FRC was 'the subject of or pending review' was allowed by BIS officials under delegated authority.

21 See comparison of Company Law and FRC 2014 True and Fair guidance
22 ONS FOI 2017/3410 whole FOI and doc 59 summary
23 HL 4991

8.4 One is left to wonder what arrangements and leverage was going on, but after the ONS reconfirms in 2010 that the FRC should remain a public body, an email note from HMT[24] continues to press for a change, saying: '*[T]o do anything else may result in the FRC raising this at a very senior level and/or taking some radical steps such as seeking a judicial review, which could be embarrassing for all concerned*'. Whether or not that was an idle threat, there is a great deal that is embarrassing about the FRC's status and conduct.

8.5 So, the FRC has been far from timid in defending itself and own interests; for example, the 'true and fair' issue with LAPFF where, in collusion with officials at BEIS, FOI disclosures[25] relating to that matter [10 July 2013, FOI page 10] show an operation seemingly mounted to canvass support for the FRC view. A BIS official stated, concerning a joint commissioning of the Moore Opinion: '*[T]his is not enough on its own: we need to be thinking how to engage with, and hopefully convince, as many of the investors as possible*'.

This is a revealing statement that is made before the opinion has been obtained.

8.6 Then, after a **draft** opinion has been obtained, a statement from Richard Fleck of the FRC to BIS reads: '*We have now developed the Martin Moore Opinion to an advanced stage and I thought it would be useful to share it with you to see whether you would like to discuss any points or seek the inclusion of any points*'.19 September 2013 page 30[26]

8.7 Given that I found this consultation and collaboration on an Opinion a little strange, I submitted a PQ asking to see the Instructions to Counsel[27]. I was told in the reply that they are confidential and that, despite the obvious involvement of BIS from the FOI emails, the Government did not ask to see the instructions. I found the nature of this confidentiality curious: apparently, the public is allowed to see the answer from Martin Moore QC, but not the questions he was asked to address.

8.8 Then, when the opinion is finished, we can see in the same FOI on 2 October 2014, page 14 an official from the FRC asking BIS: *'[C]an you get on to your oppos at the ABI and IMA this afternoon please to drum up some support. And as they will be asked, can you brief the Big 4, the ICAEW, 100 group and the IASB. We may want investor comments more, but let's ensure we get the profession and corporates on our side'.*

8.9 Getting it wrong seems to be a strength of the FRC. From that starting point, it then presses ahead with its own view whether correct or not. This can be seen in email exchanges[28] where the FRC told journalists that BIS had said that LAPFF were wrong. BIS in fact denied saying that. Stephen Haddrill repeated the same line to the House of Lords. It

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24 ONS FOI 2017/3410 doc 44
25 See attached BIS FOI 2016/15803 (page 10)
26 BIS FOI 2016/15803
27 HL 5215
28 BIS FOI 2016/07497

can be seen in the FOI that BIS officials are very careful in what they get the Minister to sign off.

8.10 On occasions, the FRC has claimed it lacks the power it needs to take action. Stephen Hadrill stated this to the Joint Select Committee hearing only for the Secretary of State to contradict him: '*I do not agree with Mr Haddrill that there is something that is preventing vigorous action being taken, and my expectation is that they will work with their fellow regulators*.'

8.11 The FRC also prepared Appendix lll to its guidelines summarizing and interpreting the disclosure requirements of CA2006. Some of the interpretation was unhelpful. For example, guidance on the strategic report was to '*only report on those matters that are of direct relevance to shareholders'.*

8.12 The guidance used to say '*The guidance also encourages companies to focus on the application of materiality to disclosures' which implied financial materiality.*

8.13 Client Earth in evidence to the BEIS Select Committee criticised the FRC for failing to improve strategic reporting.

8.14 The FRC was on the wrong side of the argument on all these issues although, following pressure, including from myself, changes have been made (such as to include non-financial materiality). But it did not happen until the spotlight was upon them; culturally, they were again in the wrong place.

8.15 The FRC has provided guidance[29] concerning the new s172(1) reports that are required from next year. It is too soon to provide analysis in depth, but initially it seems (possibly) to have imposed a materiality requirement (limiting to strategic matters) that is not in the new CA s414CZA provision in the new 2018 Regulations. The new provision appears to flow directly from the director's report in s416(4) and not from the strategic report. Confirmation of this seems to be in another provision of the guidelines which point out that the provision allowing withholding of prejudicial business interest does not apply – which it would if it were under the strategic report.

Q9: Are there changes respondents would like to see to achieve the vision set out in the Review's terms of reference?

Yes. Create a proper companies regulator with a proper statute and without conflicts of interest. It does not seem likely that the FRC can be 'fixed' without eliminating all the collaborative tenets, and those holding them, on which it was founded and has been operating. The combined summary recommendations are:

[29] FRC Guidance on the Strategic Report 2018

Remove the market-led collaborative structure in both set up and culture

The FRC, or its successor, needs a more compelling mission of enforcement that includes a direct duty of care for the public interest.

The FRC/New Regulator must be set up by full statute for all its activities. The statute should embed the duty of care for the public interest as well as the primacy of company law over any other standard setting or guidance

Possible merger with the Insolvency service and Companies House, but in any event give audit discipline to the Insolvency Service.

Remove accounting standard setting to an independent body (also actuarial standards)

Less reliance on accountancy/audit professions in its committees and boards

The combination of structure and functions must be such as to ensure audit can challenge, not be a slave to standards or caught in a feedback loop of marking own homework

Q10: Are arrangements for financial reporting, audit and corporate governance the critical elements for effective delivery of FRC's mission, or are elements missing?

10.1 Non-financial reporting must also be included.

10.2 The FRC/New Regulator must not set accounting standards and also regulate auditors.

10.3 Company law should always be followed with care.

10.4 Serious consideration must be given to whether voluntary corporate governance codes should remain with a regulator.

<u>Audit regulation</u>

Q11: How effective is the FRC at driving quality improvements in audit? What further improvements would respondents like to see?

11.1 The FRC has been part of the problem.

11.2 Parliament seems to have been the body that has stepped in to force up standards, first with banks (although the role of auditors in the financial crisis and issues such as true and fair have not been fully thrashed out) and more recently after BHS, Carillion and others.

11.3 The FRC/New Regulator should be looking ahead to identify and test or challenge emerging trends.

11.4 The FRC/New Regulator should aim for audit to pick up problems before they get worse. In Barings, the Judge criticised auditors for letting Nick Leeson's debt run up above

£1m – these were small numbers compared with the HBOS escalation over a matter of months.

11.5 The recently commenced preparedness to criticise the Big 4 and be a bit bolder should continue – not be dropped once the current FRC crisis has passed.

Q12: Where quality does fall short, do the FRC's interventions have sufficient impact and deterrent effect?

12.1 No. In general, matters seem to have got worse rather than better, so interventions (whatever they may have been), and punishments, do not appear to have had any effect. We can only hope that some of the recent fines and bans will have an effect. But whether the FRC will remain willing to use those sanctions – and frequently – remains to be seen.

12.2 The weakening of the standards by which auditors are measured should be reversed.

12.3 Consideration should be given to use of a senior manager regime within audit firms.

12.4 An examination of director responsibility would also be worthwhile. The Select Committee recommended that investigation and punishment should not just fall on those with accounting qualifications but on all those who exert influence. There are more general issues of corporate liability that are beyond the scope of this review but which are nonetheless highly relevant to corporate behaviour.

12.5 It might be useful to have a procedure to determine routinely when to investigate directors for the purpose of recommending to the Secretary of State that he or she exercise power to disqualify directors under the Company Director Disqualification Act[30].

Q13: What force is there in the concern of some that the FRC may be too close to the "big 4"? Or that the FRC is too concerned with the risk of failure of one of the "big 4"?

13.1 Being too close to the Big 4 is a valid concern. There are collaborative arrangements, as referenced in the ICEAW article[31], and the presence of senior members of those firms within the FRC to consider. In formal links it appears more concentrated with regard to PWC and KPMG.

13.2 The fact is that the Big 4, and especially the Big 2, are omnipresent throughout Government and business, through advisory work and secondments as well as in accounting and audit, and that their former employees are spread widely – including at the FRC. This gives an unconscious bias whether or not there is any specific deference or collaboration. It does seem beyond coincidence that issues around the Financial Crisis have not focussed on audit.

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[30] As amended by the Small Business, Enterprise and Employment Act 2015
[31] ICAEW April 2018 as before

13.3 In personal discussions with the FRC and Stephen Haddrill, I have been made aware that they have concerns about risk of failure and lack of competition, with a sense of 'But what can we do?' It may also be the case that this has inhibited them from rocking the boat or that, at least until recently, their collaborative arrangements meant that they would prefer others to do the rocking.

Q14: Are investigations of audit work effective, transparent, satisfactorily concluded and unfettered?

14.1 There are certainly some investigations that have not been satisfactory such as BHS, HBOS and Carillion. The way in which the FRC works generally lacks transparency and so whether investigations are unfettered is hard to know.

14.2 With both Carillion and the Co-Op, the FRC seems to have passed as satisfactory things that it should not have cleared had it looked more closely.

14.3 Measured by results, the answer has to be that the FRC is ineffective because standards of audit have not improved. Either the checking is not good enough or there is no significant fear of reprisals – save for the very recent stricter fine and disqualification that has occurred since the FRC fell under the spotlight.

14.4 Transparency could sometimes be inhibited due to legal issues. This is something that should not be overplayed but may need investigation and some legislative correction.

14.5 The previously mentioned feedback loop of audit being deemed 'satisfactory by process' (accounting standards), and the FRC having responsibility for accounting standards, means that there is potentially a conflict of interest and, perhaps, an inherent reluctance to look beyond the standard.

Q15: Could a different regulatory strategy or tactics result in greater avoidance of harm?

15.1 Yes. A stronger regulator that is well resourced, acts truly in the public interest rather than being answerable to those it regulates, is free of conflicts and which uses expertise and governance drawn from beyond the Big 4, listed companies and City law firms that act for them would make a difference.

15.2 There should be a mechanism to challenge audits and tardy or missing regulatory action. Having an Ombudsman to deal with justified complaints about lack of regulatory action might help as it is almost impossible to challenge a company, even for shareholders via a derivative action. Moreover, the public has no locus nor protection if the regulator is weak.

15.3 As previously mentioned the New Regulator should be looking for ways to protect the public by investigating new behaviours and trends and acting to avoid problems from escalating.

Q16: Could or should the FRC's work promote competition and a well-functioning audit market? Does the FRC's work undermine competition or a well-functioning audit market in any way?

16.1 The regulatory role is to oversee and enforce high-quality audit, it is not a competition authority. However, it should certainly avoid doing things that cause harm to competition and should be strict on achieving things that might assist. The FRC/New Regulator should have a role in oversight of audit rotation and the level and type of advisory work done by audit firms. Legislative revision of that issue is desirable because only the minimum has been done so far.

16.2 In historical terms, the FRC has contributed to the reduction in competition through the extension of IFRS beyond the group level. The extension of IFRS into more areas renders accounting and auditing more complex giving rise to a need for a great deal of continuing advisory work. That has generated work that is to the advantage and profit of the large firms, which also get involved in the standard-setting process, and has put much work out of the reach of smaller organisations.

16.3 Reappraising where IFRS must be used is essential – but by another body, given that standards should be separate and because it was the FRC's decision to apply it to subsidiaries.

16.4 Reviewing whether to continue with IFRS other than for group accounts merits consideration in its own right, although it might also open the way for use of non Big 4 for subsidiary companies.

16.5 All the ideas surrounding the break-up of the Big 4's dominance need to be revisited, and it is to be hoped that the Competition and Markets Authority will do this and produce stronger outcomes than before – given that audit rotation has done nothing.

16.6 The FRC should engage with the PRA about its opposition to allowing auditor selection from outside the Big 4.

Q17: Can questions regarding the effectiveness of the FRC be separated from the wider question on whether change is needed to audit arrangements to take account of shifting expectations?

Issues:
- Requires a strong unbiased regulator
- Enforcing the law as intended
- Possibly regulation to aid reinstatement of prudence and judgement
- Address the separate financial statements and IFRS issue
- Are expectations shifting or is it falling standards?

17.1 Yes, to some extent and both need to be addressed.

17.2 The, FRC is flawed in its structure and culture and that has, if not contributed to, then at least permitted the undermining of standards by dubbing inadequate audit as an 'expectation gap' – as if expectation has increased. What is required by law has not changed; however, it needs to be properly enforced in a way not contaminated by bias (unconscious or otherwise) or misdirected through following a standards-driven process.

17.3 What has perhaps changed in perception is the realisation that it is impossible for investor stewardship to be sufficiently thorough (on the basis of an annual report) or for the investor's scrutiny to represent the public interest.

17.4 In just the same way that amendments have been made by new regulations to s172 reporting, in order that it is enforced as Parliament intended, it might be necessary to regulate so as to ensure audit functions as intended, as well as requiring judgement as an expectation.

<u>Accounting and financial reporting</u>

Q18: Has the FRC been effective in influencing the development of accounting standards internationally as well as accountable and effective in setting UK GAAP?

18.1 The FRC has been effective in promoting IFRS, but it has not been effective in preserving the requirements of company law. Indeed, the FRC was in the vanguard of seeking to drop prudence[32].

18.2 Evidence was given to the House of Lords Economic Affairs Committee in 2014 about attempts to reinstate prudence in IFRS. The apologetic responses that Stephen Haddrill made in evidence on 22 July 2014 hid the fact that changing IFRS was not the only solution. IFRS was only required by the EU at group level; it was the FRC that pushed it down to below group level where prudence issues could otherwise have been retained with significant effect in separate UK GAAP financial statements.

18.3 One of the reasons that there is little international sympathy/support for the UK to change IFRS is because other EU countries do not apply IFRS to separate financial statements. So they say, 'You can fix it for yourself'. Equally, other countries introduce their own additional measures as Australia has done. The UK is a victim of its own rules here. Nevertheless a proper ***audit*** looking at substance and ***using judgement*** should go beyond accounting standards and pull out underlying disguised debt, such as Carillion's reverse factoring and the risk that it entails.

[32] FRC Letter 8 April 2005 again

18.4 The fact that audit must challenge where standards conceal is why the same regulator should not set accounting standards and have responsibility for auditing.

Q19: How else could the FRC improve the quality of financial reporting with a view to ensuring investor confidence?

19.1 The FRC/New Regulator must return to the prudent approach. Audit must challenge, not be standards driven.

19.2 The FRC should encourage more qualitative reporting. Some of this is starting to happen, although it is a pity that the history of the FRC has been to give guidance that led away from it.

Q20: Are there wider issues of financial and other reporting on which a stronger regulatory role would be desirable to better meet the information needs of investors and other stakeholders?

20.1 Companies must be made to report thoughtfully not by tick box and standardised paragraphs. FRC guidance should not lead in that direction.

20.2 Companies should be required to rewrite reports if they are inadequate, explain why if it is fundamentally a copy and paste of the previous year, and highlight changes.

20.3 The new s172(1) reporting should be properly monitored, including for subsidiaries and private companies. The FRC/New Regulator should be responsive to concerns when they are raised so that there can be a 'many eyes' checking that is effective beyond FRC checks. The guidance that has been offered by the FRC must not make suggestions for bland catch-all statements that will be used by rote.

20.4 The reporting of, adherence to, or departure from the corporate governance code should be monitored and fuller explanations given where there is non-compliance. The level of disclosure should be much more along the lines of seeking a derogation than a statement that it 'Just doesn't suit'.

20.5 The Code may be better done by a different entity, although consideration should be given as to whether comply or explain is past its sell by date. It was only really brought in to pander to a few large companies that did not want to have independent chairs or separate CEO and Chair. It followed that they did not and the Code made no difference. Experience shows it is regulation and reporting requirements that bring change – we have seen this with executive pay, gender diversity and payment practices.

20.6 The very restricted way in which director's duties and reports can be legally challenged only by shareholders and through a derivative action needs attention to make shareholder challenges realistically possible. This extends beyond this review into corporate liability, although it is an important part of the picture.

20.7 The difficulty of taking derivative actions means that the regulator's role is even more important in terms of capacity and willingness to respond to complaints and make investigations.

20.8 Failure of the regulator to take action should be capable of challenge, for example, through an ombudsman. This ombudsman could also serve as a route for stakeholders to make complaints about a company. A mechanism for public complaints should also be envisaged --- possibly by petition.

Q21: Is the current combination of statutory and voluntary methods of oversight for professional bodies effective, and do they remain fit for the future?

21.1 No. Oversight of such fundamental professions should be statutory.

<u>Corporate Governance and Stewardship Codes</u>

Q22: In relation to the UK Corporate Governance Code, are there issues relevant to the Review's terms of reference that respondents believe the Review should consider?

22.1 As in Q20, it might be appropriate to consider in the light of any proposed new FRC/New Regulator remit whether a regulator that monitors compliance with company law on a proper 'comply or else' basis should also prepare a 'comply or explain' codes. It sets the scene for a continuing weak regulator and mixed messaging. If it is retained, it might be necessary to remove it from the regulator, as is the case in Australia.

22.2 As I have stated above, the comply or explain model was largely brought in to satisfy a few large companies that continued to have either a joint chair and CEO, or which lacked an independent chair. Such issues could be dealt with by a 'permission to derogate' that is then reported alongside reasons in the annual report.

22.3 It should be examined how much of the Code really should be an absolute requirement and how much is a code version of those things nobody dares to say should be mandatory.

22.4 The role of the Listing Authority could be expanded in this matter including on the quality of the reporting of compliance.

Q23: How effective has the Stewardship Code been in driving more and higher quality engagement by institutional investors? If not, why? How might quality of engagement be further strengthened?

23.1 The problem with the Stewardship Code is that little is known about what is being said in specific terms by institutional investors, so the end investor, the public, does not know.

23.2 The matters on which there has allegedly been most engagement, such as remuneration, director diversity and consideration of stakeholders have required other reporting measures to make an impact. So although it is better than nothing, the evidence is that things only happen when there is a legislative requirement such as reporting on pay, gender, payment practices and s172 duties.

23.4 There is also a conflict where the institutional investors themselves have highly paid executives or the same type of corporate set-up and governance shortcomings.

23.5 It might be better than nothing, but it is not a solution for deficiencies in regulation and enforcement and has been used as an excuse to stave off tougher-but-necessary corporate-governance measures.

Speed and effectiveness of investigations; enforcement and compliance

Q24: Do respondents view the FRC as reluctant to undertake investigations or enforcement, or able to do so at speed?

24.1 Yes. I would like to know whether and why there has been any undue influence or fear of consequences or litigation or budgetary constraints. All should be attended to.

Q25: How could the FRC better ensure it is able to take swift, effective and appropriate enforcement action? What practical or legal changes would be needed to achieve this?

25.1 This requires a reformed regulator, without conflicts as elaborated in other sections, and better funding so that enforcement begins in a timely manner.

25.2 The FRC has raised concerns about the Companies Act confidentiality requirements. It is not appropriate to need permission from auditors and the company's permission before making public statements, although a notice period is appropriate to give time for a right of reply. This might require a legal change.

25.3 Consideration could be given to a maximum time period for retaining any confidentiality concerning an enforcement action, after which information concerning a pending enforcement action and the nature of the action shall be disclosed.

25.4 More generally, investigations need to be made into the use of litigation to delay and frustrate regulatory enforcement including publication. This is a problem faced by other regulators.

25.5 There are times when public information on UK companies is first available from SEC filings. The UK regulator should be in a position to disclose anything that would be disclosed by the SEC.

Actuarial oversight

Q26: Have the arrangements put in place following the 2005 Morris Review stood the test of time, or is there a need for change? Should actuarial regulation be a focus for the Review's work?

26.1 The same comments could apply as have been made for accounting with regard to separation of standard setters and regulators/auditors.

26.2 The actuarial role in the demise of Equitable Life should not be forgotten.

FRC and corporate failure

Q27: Is there more the FRC could or should do to help reduce the risk of major corporate failure?

27.1 Yes, more should be done. But it is unlikely to be effective until the issues of capture, culture and conflict are addressed.

27.2 Restore prudence into accounting standards at least at subsidiary level. This can be done without breaking from IFRS at group level. I do not accept that the so-called reintroduction of prudence into the latest iteration of the IFRS Conceptual Framework amounts to anything other than window dressing. More than that, its reintroduction has been done in such a way so as to avoid creating an obstacle to future US adoption of IFRS. At best, it leaves the situation as Paul Tucker described (see also 32.3), having to somehow deal with the missing corporate solvency.

27.3 Apply fully and routinely the primacy of company law to audit rather than relegate it to a 'just in case' override for special circumstances.

27.4 Investigate and flag up new procedures – especially where accounting standards throw up anomalies such as reverse factoring. There must also be requirements not only to flag up these issues but to specify the underlying effect.

Q28: Is the FRC quick and effective enough to act on warning signs arising from its work on accounts and financial reporting, or on evidence of concerns over poor corporate governance?

28.1 No. The FRC seems to have given the 'OK' to things that are far from OK, as with the Co-Op and Carillion. It has put matters to bed rather than raise concerns.

28.2 Where auditors do flag concerns, they must be monitored in the case of the largest companies. We must not wait for the next annual report or disaster.

28.3 In the case of a large company, its auditors should be obliged to report concerns to regulators. Such an arrangement used to exist with the Bank of England for banks.

Q29: Is there a case for a more "prudential approach"? If so, how could this operate in practice, and to which category of company might such an approach apply?

29.1 There have long been concerns about the removal of explicit references to prudence from accounting standards. There is a first case to say 'restore' to firm application what is already required in company law.

29.2 Company law requirements should be separately reported and more clearly elaborated in audit with a narrative of how they have been investigated/applied. It should be noted that Company Law s393(1) refers to a true and fair view of the assets, liabilities, financial position and the profit or loss. This is more granular than the FRC's 2014 True and Fair guidance, which refers to viewing accounts as a whole.

29.3 Attention should be given to the prudential regime of Part 23 of the Companies Act 2006 that some institutional investors have highlighted.

29.4 Listed and large private companies could be required to report more frequently on solvency in order to catch problems sooner. This could be a procedure that is triggered by particular circumstances.

29.4 As in 28.3, auditors reporting concerns to regulators.

Q30: Introduction of the viability statement was an important development, but could it be made more effective?

30.1 The viability statement does not seem to have picked up as much as was hoped and in many instances has become a standardised statement. More narrative on the analysis and conclusions should be required. Some companies have done it much better than others.

30.2 Consideration should be given to stress testing scenarios for large/systemic companies.

<u>**Powers and sanctions**</u>

Q31: Are there gaps in the FRC's powers? Would its effectiveness be improved with further (or different) powers?

31.1 It is not entirely clear what the FRC powers are. The chief executive of the FRC has told select committees that it is one of the most effective and respected regulators in the world. This is not a view that I ever had expressed to me from outside the UK. He has gone on to say that it does not need any more powers (in an individual meeting and also to an APPG). However, a short time later, he subsequently told the joint Select Committee hearing that it does not have power to act effectively in some instances. The Secretary of State, however, argues this is not the case and says that he expects regulators to work together.

31.2 This shows that the situation is confused and must be clarified. The FRC/New Regulator certainly needs to be able to seek changes to all aspects of the annual report and be willing to pursue that.

Q32: Are the FRC's powers coherent in relation to those of other regulators?

32.1 Who knows? At the same time as the Secretary of State said regulators must work together, reference was made to a memorandum of understanding being drawn up between regulators. I have been unable to find out anything about it. The memorandum should be published.

32.2 PQ HL6568[33] (among several others on the matter) states that the supervision of the accounting solvency of the Companies Act 2006 is supervised by the PRA. PQ HL 6970[34] states that the auditor responsibilities do not differ. There clearly can be interaction here between PRA supervision and audit quality overseen by the FRC. The PRA issue over Goldman Sachs wishing to appoint a non-Big 4 auditor might be an example.

32.3 The comments of Paul Tucker to the House of Lords[35] EAC (Mervyn King also giving evidence) signalled an awareness of problems with the accounting measures of solvency. He stated: '*[A]nd therefore its company law measure of solvency is exposed*'. Lord Lawson queried why auditors had failed to raise a red flag with the 'huge expansion of balance sheets', to which Paul Tucker replied: '*As the Governor has said, it's hard for us to know how close or not close they were to the audited firms during that period, because it wasn't part of our formal responsibilities at that time.*'

Q33: Taking account of Sir Christopher Clarke's review of sanctions, and subsequent changes, does the sanctions regime now have the right deterrent effect? Does the FRC make best use of the sanctions at its disposal?

33.1 The answer to this seems to be no from the circumstances recently seen, although the very recent increases in fines are to be welcomed.

33.2 The oversight arrangements the FRC relies upon seem to be voluntary ones rather than the full range of sanctions (including criminal ones). This is why the Insolvency Service may be a better regulator for auditor discipline, as well as putting some separation from the standard setting body.

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[33] HL 6568 see also HL 6193 and HL 5823
[34] HL 6970
[35] Economic Affairs Committee 16 November 2010

FRC's legal status and its relationship with Government

Q34: Should the Government legislate to put the FRC on a more conventional consolidated statutory footing?

34.1 Yes, this is essential alongside the changes to culture and conflict, otherwise there is too much risk of slippage and 'interpretation'.

34.2 The FRC is classified as a public body by function, and always has been, but only recently has this been conceded by its sponsoring department. Any legislation must not be half-hearted and try to preserve the current habits. It needs to be a new regulator not a statutory version of the current arrangements.

Q35: What is the optimal structure for the relationship between the FRC and the Government, best balancing proper accountability with enabling the FRC's effectiveness?

35.1 The statute should make clear the duty of care for the public interest exercised with the derogation of power from the Secretary of State

35.2 Like other UK regulators, it should be independent but accountable to Parliament.

35.3 Powers and functions should be separated out between regulators so as to make sure they are not in conflict. Standards and audit should be separate and ideally so should enforcement, such as in the Insolvency Service, or at the very least be in an autonomous arm if, for example, there were merger with the Insolvency Service under a company regulator umbrella.

35.4 There should be an end to the notion that the FRC/New Regulator can be effective as a consequence of voluntary and collaborative arrangements.

Q36: In terms of the FRC's broader accountability, is there a case for further transparency in its actions or functions?

36.1 The FRC has been very far from transparent concerning itself and has done everything it can to preserve that as part of resisting public body status and accountability. This has to change and FOI should apply on a maximalist basis, unlike at the present where it is minimal.

36.2 With regard to its actions the balance must always fall on the side of transparency and against confidentiality because the law must be seen to be applied and investigations seen to take place. If necessary, legal changes should be made.

Governance and leadership

Q37: How effective is the current leadership and Board of the FRC? Please cite relevant evidence which informs your view.

37.1 The leadership of the FRC has been complicit in the issues of culture and outlook, at times seeming to campaign against the law[36]. Notable issues are the classification saga (culture), True and Fair (collusion to get opinion it wanted on interpretation, now effectively acknowledged to be wrong[37]), and the promotion of neutrality over prudence through the IASB (against company law, poor judgement).

37.2 The current CEO was instrumental in, and heavily invested in, the 2004 changes to the FRC. He has presided over repeated attempts to obtain private-body status for the FRC rather than move on to a modern, accountable, non-captured framework. This has fostered the inadequacies that have come to light. There seem to have been an unusual number of unfortunate coincidences, from praising companies that almost immediately have problems to board or committee members coming from companies that then get into difficulties.

37.3 The CEO is overseen by his wife at BEIS and neither of them seemed to think this was a matter of conflict[38]. That is very poor judgement for a leader of an organisation intended to lead good behaviour. The conflict of interest register has only recently been introduced and is minimal. Overall, he seems too vested in interests of the past to be the one to lead a new or reformed organisation.

37.4 It is a mistake to have as chair – and in other significant board or advisory positions – individuals who have held positions of responsibility that give rise to conflicts of interest. Given the unexplained and unexplored role of accounting standards and audit in the financial crisis, it must be a mistake to have individuals who were at the heart of the crisis and aftermath in key regulatory positions. The chair should be far more independent of events of the financial crisis, companies, professions and the City in general. **The chair should be there to give comfort to the public not to companies.**

37.5 To have as chair an individual who was chair of Lloyds and under challenge with regard to knowledge of the HBOS fraud makes his position even more untenable.

Q38: Is the Board's composition appropriate? Is it the right size? Does it have appropriate membership?

38.1 The answer must be no, because it has not worked. Recent 2018 appointments of more women and with different backgrounds are welcome, but much more of this kind of diversity is needed throughout the organisation.

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36 FRC 8 April 2005 letter
37 Walker -Arnott Journal of Business Law Issue 6 2017, also HL 5280
38 Reported in The Guardian

38.2 More generally this should be a matter for legislation, but having a board substantially drawn from those regulated, one way or another, or closely related to those regulated, has to be wrong.

38.3 It is also unclear from minutes whether the board has been able to exercise sufficient oversight.

38.4 It is not clear, given the history, what the term in paragraph 36 of the call for evidence ‘the determination of risks to the FRCs strategic nature’ means. It could echo the notion that it is about attracting business rather than good regulation. In other words the old FSA-type problem. The board should be concerned with lawful regulation and enforcement and recognise the <u>systemic</u> nature of the role it plays.

Q39: Is the balance of decision-making between the Board, its Committees and the Executive described in paragraphs 34-36 above right, given relevant legal constraints?

39.1 The FRC structure suffers from its concept as a collaboration and, in consequence, from where it draws its expertise and sets its strategy. This permeates its committees and boards so the problem is one of fundamentals rather than specific set-up. A new regulator should be established that avoids these problems and conflicts.

39.2 There should be restrictions on how long individuals can serve collectively on the board and committees. The same people should not just rotate around for an indefinite time.

39.3 The 2012 changes aimed to resolve some conflicts and mean that the Board is no-longer responsible for the opening of investigations. In the interests of independence of enforcement, this is a positive development. However, perhaps the Board should have an override to open (but not prevent) an investigation? This might, of course, be unnecessary if enforcement is separated out completely.

Q40: Is the Board’s structure appropriate, including given the FRC’s roles on standard setting, assessment and enforcement? Does the Board’s accountability appropriately reflect its role and functions? Are its decisions appropriately transparent, bearing in mind the need to balance public interest and confidentiality?

40.1 The FRC/New Regulator should not set accounting standards. The structure is inappropriate in that regard.

40.2 Independence of enforcement is important. There are arguments that it should be completely independent. Questions still remain as to why there has been a failure to open investigations. The answers to these questions might have more to do with culture, strategy and, possibly, the inclinations or interests of the individuals who control decision making than with the board structure.

40.3 Transparency is poor. Confidentiality might well have been over used and so when it is invoked, it must be justified. The balance of 'public interest against confidentiality' has been far too much against the public interest.

40.4 Current accountability is completely wrong as because it is accountability to the collaborative structure that has led to a captured regulator.

40.5 Compliance with the law under regulators is strongly related to justice, which is public, and which must be seen to be done. Markets and the public need to know when there are issues that raise flags. That would be a huge incentive for companies to perform better rather than rely on a cloak of confidentiality. And why not? It would also mean that the regulator must be diligent in the conduct of the investigation. This is all the more the case when the prevailing questions that are asked are 'How was this allowed to happen?' and 'What was the FRC doing about it?'

Q41: How should the Executive's effectiveness be assessed and ensured?

41.1 The present behaviour should be assessed against the standards and culture that it is in charge of promoting, and against standards for public bodies and standards of public life. They appear to have fallen well short on both.

41.2 There should be full reporting to Parliament. I could not locate the annual reports that the FRC says it provides to Parliament.

<u>Funding resources and staffing</u>

Q42: Who should fund the FRC, and how? What are the impacts of current funding arrangements, including of having a partially voluntary funded regime?

42. 1 Funding should be compulsory. It was made voluntary as part of the 'collaborative' set up, because, in the words of the FRC letter[2] 'they pay for the influence that they get', and also as a reason to say it was a private body. It is at last properly acknowledged, whatever its form, as a public body by function and the days of pay for influence must go.

42.2 Funding for oversight of auditors should come from a levy on the profession.

42.3 Accounting standards should be in a separate body, funding for which could come from the bodies that use them, which includes those firms that generate income from advisory work and related to that income.

42.4 Combining with Companies House would also give other possible sources of income reflecting that some of the work is general for all companies.

Q43: What skills are needed for the FRC to be most effective? Does the FRC have the people, skills and resources it needs, of the quality it needs?

43.1 The FRC is too influenced by practitioners and the corporate view and lacks sufficient instinct for or knowledge of protection of the public interest.

Q44: Are there conflicts of interest in the FRC's structure, processes, or culture? Are there deficiencies in the FRC's approach to managing conflicts of interests?

44.1 Yes. See all the above. It is hard to design a set up that is more captured and where that has been lauded as a strength. There are conflicts by design and a vehement unwillingness to do anything about it.

44.2 The register of interests was only relatively recently set up after criticisms. Even then it did not disclose much. For example, there is no disclosure of shareholdings or other financial interests. There is also no disclosure of how conflicts are managed and an apparent unawareness of where conflicts lie. An example is the failure to recognise even that having the CEO overseen in BEIS by his wife is an issue.

44.3 Within the FRC, there is astounding lack of awareness of the true perception of the FRC or how it is viewed.

<u>Other matters</u>

Q45: Are there any other issues relevant to the terms of reference that respondents would like to raise?

There is a large body of documentation from my Parliamentary Questions and from Freedom of Information requests to the ONC and BIS and refusals of FOI by the FRC that tell a sorry tale of defending the indefensible at a time when the failures of the indefensible operation are coming to light.

The references given in this evidence are only examples and more documentation is available. Regretfully, departmental officials also seem to have been partisan over FRC matters. Serious policy issues have not been resolved and in particular with regard to BIS FOI 15803, which went to appeal, it may be instructive for the inquiry to see unredacted versions.

The only way to resolve this is to start again so that people are not defending their vested interests. There may well be issues that require further investigation.

References and notes index

References	PDF and Location
1 ONS FOI 2017/3410 Doc 16	Bowles 1 ref 1
2 ONS FOI 2017/3410 Doc 42 – FRC December 2004 letter	Bowles 1 ref 2
3 ONS FOI 2017/3410 doc 59	Bowles 1 ref 3
3 **Full ONS FOI**	**Bowles refs 2**
4 FRC Strategy 2018/21 foot of page 8 (see website)	Bowles 1 ref 4
5 ONS FOI document 59	same as ref 3
6 HL 8896 (all HL PQs, including those not referenced)	Bowles 1 ref 6
7 HL 4991	see under ref 6
8 HL 7591	see under ref 6
9 HL 9366	see under ref 6
10 MoU between FRC and BIS	Bowles 1 ref 10
11 HL 4990	see under ref 6
12 HL 6436	see under ref 6
13 FRC letter 8 April 2005	Bowles 1 ref 13
14 HL 5280	see under ref 6
15 FRC Minutes	Bowles 1 ref 15
16 eg HoL EAC Q197 2010, 22 July whole evidence session (public document)	not provided
17 FRC December 2004 letter	same as ref 2
18 April 2018 article icaew	Bowles 1 ref 18
19 Lords EAC 16 November 2010 (public document)	not provided
20 FRC 8 April letter	same as ref 13
21 Comparison Law and guidance	Bowles 1 ref 21
22 ONS FOI 2017/3410 doc 59 summary	same as ref 3
Full ONS FOI	**Bowles refs 2**
23 HL 4991	see under ref 6
24 ONS FOI 2017/3410 doc 44	Bowles 1 ref 24
25 ONS BIS FOI 2016/15830 (page 10)	Bowles 1 ref 25
Full BIS FOI 15830	**Bowles refs 3**
26 BIS FOI 2016/15803 (pages 30 and 14)	Bowles 1 ref 26
27 HL 5215	see under ref 6
28 BIS FOI 2016/07497 – pages 3-5 and 45-47	Bowles 1 ref 28
Full BIS FOI 07497	**Bowles refs 4**
29 FRC Guidance on the Strategic Report 2018 para 8.12 page 59	Bowles 1 ref 29
30 note only	note only
31 ICAEW	same as ref 18
32 FRC letter 8 April 2005	same as ref 13
33 HL 6568	see under ref 6
34 HL 6970	see under ref 6
35 Lords EAC 16 November 2010 (public)	not provided
36 FRC 8 April 2005	same as ref 13
38 Walker-Arnott, Journal of Business Law, Issue 6 2017 also HL 5280	Bowles 1 ref 38 p1
Full reference	**Bowles 5**

39 Note	note only

Document files provided

1. PDF Bowles refs 1	key wording references as indexed above
2. PDF Bowles refs 2	FOI ONS 2017/3410 zipped
3. PDF Bowles refs 3	FOI BIS 2016/15803
4. PDF Bowles refs 4	FOI BIS 2016/07497
5. PDF Bowles refs 5	Full document of Walker-Arnott ref 38