Quality and Effectiveness of Audit Review

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Dear Sir/Madam,

The Quality and Effectiveness of Audit – call for views

BP is an integrated Oil and Gas company headquartered in the UK with operations in over 70 countries. We have a primary listing on the London Stock Exchange and a secondary listing in the US.

The consultation notes that the review is primarily focused on the purpose, scope and quality of audit and not on the role of the regulator or the audit market, which are being addressed via the Kingman Review and the CMA market study respectively. We agree that that the results of the Kingman Review and CMA market study will "have considerable relevance for the quality and delivery of the audit process and product". The results of these reviews need to be implemented together, to ensure that the external audit is of a high-quality, meets the needs of its users' and operates in a well-regulated and efficient market.

The call for views outlines a number of areas where the external audit scope or reporting can potentially be expanded. Several of these go beyond current company reporting requirements. Any reporting changes to better serve the needs of users should be driven by changes to corporate reporting requirements and not by changes to the external auditor's requirements.

The external audit is one element of assurance well informed investors and other stakeholders use when assessing a company for investment or credit purposes. Investors and other stakeholders still need to assess the company's strategy and ability to execute in the context of the prevailing market conditions, using the audited accounts as a reliable source of information for track record to date and resources available to the company at the time the accounts were published. The role of an auditor is to verify that past performance has been reported correctly, rather than forecast future performance. Given the significantly different knowledge and skill requirements, this role is best performed by independent equity market analysts and credit rating agencies.

Our response is set out below against the consultation questions provided in the consultation chapters.

Chapter 1) Definitions of audit and its users

1. For whose benefit should audit be conducted? How is it of value to users?
2. Should the audit be designed to enhance the degree of confidence of intended users in the entity or just in the financial statements?
3. 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?

Response:

We support the 100 Group's response to questions 1, 2 and 3

Chapter 2) The 'Expectation Gap'

4. Do respondents consider there is an expectation gap?
5. If so, how would respondents characterise that gap?
6. 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?

We support the 100 Group's response to questions 4 and 5.

We do not propose to respond specifically to the question 6.

We agree with the observations outlined in the CMA's call for evidence in relation to an expectation gap around the purpose and scope of an audit. By its nature, an audit is primarily backward-looking. It is an essential building block in the process of assessing the financial health of a company, but on its own is not capable of preventing a corporate failure. Investors and other stakeholders still need to assess the company's strategy and ability to execute in the context of prevailing market conditions. A corporate failure is not necessarily an indicator of an audit failure nor of weaknesses in the audit product. A high-quality audit that lays out financial weakness and risk of failure still needs to be acted upon by management, investors, customers and creditors.

Chapter 3) Audit and wider assurance

7. What should be the role of audit within wider assurance?

8. 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?

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

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

11. 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?

We support the 100 Group's response to questions 7 to 11.

- In our experience the controls around independence and limitations on non-audit work are effective and we have no concerns around audit quality.

- We believe that a tender undertaken with sufficient time between selection and the commencement of the audit tenure can ensure that there are no independence limitations and all participants are incentivized to provide innovative and high-quality services.

Chapter 4) The scope and purpose of audit

Risk and internal control

12. 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?

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

14. 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?

We broadly support the 100 Group's response to questions 12, 13 and 14.

- We would support enhancing the current reporting disclosure requirements, if of benefit to users, but believe this should continue to be focused on Key Risks only.
- We support a review of the UK control regime and would also support the introduction of a UK equivalent to US SOx.
- Any changes to the UK requirements should consider frameworks already in existence, such as US SOx, and include an equivalence criterion for reporting and auditing to avoid duplication of cost and effort for no incremental value to users.
- We believe that the most effective standards are set at an international level as they are well understood and avoid unnecessary cost and duplication.

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

16. 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"?

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

18. Should such a statement be subject to assurance?

19. Who might be capable of giving such assurance?

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

21. 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?

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

We support the 100 Group's response to questions 15 to 19.

- Consideration of future factors which may impact a business are inherently more judgemental. Review of such information requires a significantly different skill set, and level of business and market knowledge than external audit.

- The going concern and viability statements are management's own assessment of future performance and the impact of external factors and trends. Users overlay this information with their own assessment of future performance and market knowledge. Expanding the scope of audit does not remove the requirement for users to perform their own independent assessment.

- Audit or assurance of financial and non-financial KPI's is possible where frameworks exist to assure against.

- Companies need to retain the right to develop their own metrics in the absence of a framework that fully aligns to their long-term objectives.

Chapter 5) Audit product and quality

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

24. 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?

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

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

27. What would prevent such disclosures becoming boiler plated?

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

We do not propose to respond to questions 27 and 28.

We support the 100 Group's response to questions 23 to 26 particularly that the introduction of graduated audit findings, which without appropriate accompanying narrative from the external auditor and management may not be of value.

Chapter 6) Legal Responsibilities

29. 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?

30. 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?

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

32. 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?

We support the 100 Group's response to question 29 to 31. We do not propose to respond to question 32.

Chapter 7) The communication of audit findings

33. 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?

34. 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?

35. 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?

We support the 100 Group's response to question 33 to 35

Chapter 8) Fraud

36. 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?

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

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

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

We support the 100 Group's response to questions 36 to 39.

Chapter 9) Auditor liability

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

We do not propose to respond to this question.

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

We do not propose to respond to this question.

42. 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?

We do not propose to respond to this question.

43. 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?

We do not propose to respond to this question.

44. 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

We do not propose to respond to this question.

Chapter 10) Other issues

Technology

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

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

We support the 100 Group's response to questions 45 and 46

Proportionality

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

We do not propose to respond to this question.

48. 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?

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

We do not propose to respond to this question.

50. 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?

We do not propose to respond to this question.

Shareholders

51. 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?

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

53. 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?

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

We support the 100 Group's response to questions 51 to 54.

Culture

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

We support the 100 Group's response to this question.

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

We do not propose to respond to this question.

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

We do not propose to respond to this question.

Cost

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

We do not propose to respond to this question.

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

We do not propose to respond to this question.

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

We do not propose to respond to this question.

Yours Faithfully,

David Bucknall

Group controller