

# Independent Review into the Quality and Effectiveness of Audit

## Advisory Board Meeting, 16 September 2019 - Summary Minutes

### Those present:

Sir Donald Brydon  
Luke Chappell  
Prof. Chris Humphrey  
Margaret Ewing  
Simon Fraser  
Mark Freedman  
Emme Kozloff  
Natasha Landell-Mills  
Michael McLintock  
Julia Wilson

### Apologies:

Carole Cran  
Alison Hopkinson  
Sarah Parkes

### Secretariat:

Miranda Craig  
Tom Barrett  
Robyn McNally  
Robin Mueller  
Paul Lee  
Mark Holmes (observer)

<b>1.</b>	<b>Introduction – agenda, matters arising and general update</b>
	<p>Sir Donald welcomed those present and noted apologies.</p> <p>Sir Donald report that he would be using his upcoming speech at the ICAEW Audit &amp; Assurance Conference on 4 October to provide some information about the responses to the Review. Following that speech, he would be winding down engagement activities to focus on preparing the final report.</p>
<b>2.</b>	<b>Capital Maintenance</b>
	<p>One issue which Sir Donald had committed to considering during his Review was that of capital maintenance, and to that end he had asked Natasha Landell-Mills (NLM) to speak for a few minutes on the topic.</p> <p>NLM thanked Sir Donald for the opportunity to address the group and set out the thinking of the group of investors of which she is part. NLM summarised her position (as publicised in a 2017 positioning paper “Investors need to know whether profits and capital are real”). The primary issue, in her opinion, is the inability of accounting standards (IFRS) to address local capital</p>

	<p>maintenance regimes, which in the UK is leading to an unacceptable risk of capital erosion through the payment of dividends based on potentially undistributable reserves (e.g. either unrealised profits and/or profits that fail to take account of foreseeable losses/liabilities left out by IFRS). She highlighted that standards bodies had acknowledged this shortcoming (IFRS is not intended to meet capital maintenance requirements) and cited the split of the audit opinion – one for compliance with standards and one “true and fair” in accordance with the Companies Act – the law having been crafted to prioritise capital protection as key to underpinning the UK’s limited liability corporate regime. Her call was for a capital protection regime to be monitored and enforced appropriately to protect investors.</p> <p>There followed a lengthy discussion on the topic, including some technical debate regarding the practical difficulties faced by companies when attempting to calculate an accurate distributable reserves amount, which was made more difficult where historical mergers and acquisition or restructuring activities had taken place. Group-level cash disclosures were also discussed, with NLM noting that investors often struggled to understand a group’s ‘true’ distributable reserve position and how much was potentially trapped in subsidiaries or in jurisdictions where it could not be utilised effectively.</p> <p>There was a debate on potential solutions, whether via enhanced disclosures or more rigorous application of existing law and standards. Some of those present were already voluntarily disclosing elements of the information under discussion or knew of others who were. There was general agreement that proportionate actions which would lead to an improved understanding of a company’s resilience and dividend paying capacity would be a good thing, but some concerns that, regardless of the actions taken, there would always be companies that would seek to ‘dress up’ their results. In addition, some were cautious of unintended consequences of any kneejerk reactions on capital markets. Questions were also asked on how responsibility and accountability should be enforced, and what role the auditor should play as well as whether auditors had the necessary skillsets to address some of the issues raised around business resilience and wider stakeholder concerns.</p> <p>Sir Donald thanked the group for the rich discussion on this topic, which he would consider when forming his final recommendations.</p>
<b>3.</b>	<b>Auditor Resignations</b>
	<p>Meeting attendees had been provided with a note summarising recent high-profile auditor resignations, together with a summary of the current requirements on auditors and companies. Several respondents had raised concerns around a lack of transparency and timeliness in the reasons given for auditor resignations. Sir Donald sought the group’s views based on their own experience.</p> <p>Attendees noted a perception that auditors often did not want to publish anything more than a bland resignation statement, for fear of putting off future clients. It was possible that litigation fears also contributed. A recent example of an unusually fulsome auditor resignation statement was highlighted, and it was noted that this statement had led to all the governance outcomes which should be expected, such as a fall in stock price and director resignations.</p>
<b>4.</b>	<b>Whistleblowing and audit</b>
	<p>Sir Donald noted that in the course of his work on the Review he had found the provisions and protections for whistleblowing employees to auditors, and auditors to regulator, unclear. It was also noted that issues around whistleblowing had been raised by the BEIS Select Committee.</p>

	<p>The meeting discussed the differences between the mechanisms available to auditors in the financial services sector and elsewhere, the extent to which there were existing whistleblowing routes potentially not being utilised effectively.</p>
<b>5.</b>	<b>AOB</b>
	<p><u>US Business Roundtable statement</u>  This statement, published recently, had been included in the meeting papers to frame a discussion around the argument (presented in the paper) that shareholder primacy is an outdated concept and was briefly discussed.</p> <p><u>Summary of responses</u>  Meeting attendees had been provided with a summary of responses and breakdown of views expressed by respondents by chapter heading, which was briefly discussed.</p> <p>There being no further business, the meeting closed.</p>