Technical Digest

January 2023

Edited by Andrew Jarvis

HAT
Group of Accountants

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WELCOME

Welcome to your January Technical Digest.

15 December 2022 was a landmark day for the profession. Not only was this the day ISQM (UK) 1 became effective, the FRC also announced their plans for significant amendments to FRS 102. These proposals (known as FRED 82) include making UK GAAP more consistent with IFRS in a number of areas, notably lease accounting, which will have a significant impact on many clients. We cover these changes briefly in this Technical Digest and will also discuss them further in our Q1 Accountancy and Audit Updates.

For ISQM (UK) 1, our support for firms continues with on demand training available for those of you who missed our live courses last year. Our pro-forma documentation is also available as part of all audit membership packages. Summaries of the resources available are here for member firms and here for others.

CPD will be a key topic this year. Many firms recognise that training is vital to develop and retain staff. Our Effective Review Workshop is a key course for anyone starting to review audit files and is taking place in London on 10 February. More generally, our Effective Supervisor and Managers courses, running this Spring cover vital soft skills necessary to develop your career. Full details are here. Separately, as you may be aware, the ICAEW are amending their CPD requirements from the end of this year. We are seeking clarifications from the ICAEW on the changes and will provide guidance for firms, including how we will support you later this year.

Finally, we are looking to expand our team with roles covering compliance (including file reviews) and in supporting and training firms more generally. Full details are here and if you are aware of anyone interested in a career supporting firms such as yours, please let me know.

Andrew Jarvis, Managing Director

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Please contact us before visiting or sending paper files for review as our London office is only open by appointment.

ISQM1

As of 15th December 2022

ISQM 1

became effective. Click below to find out more and how to ACT NOW.

Member firms click here | **Other firms click here**

UPCOMING COURSES AND EVENTS

Please see the HAT website www.hatgroup.co.uk for our full range of courses and further details such as pricing. Bookings can be made via our website or please email hat@hatgroup.co.uk or call 020 7213 9911 for more details.

CPD COURSES

The following courses are scheduled to run online over the next few months:

COURSE	PRESENTER	VENUE	DATE
Auditing in 2023: The impact of ISA (UK) 315 and ISA (UK) 240 9:30am – 12pm	Simon Kettlewell	Online	7 February 2023
Effective Audit Review Workshop 9.30am – 4.30pm	Simon Kettlewell	Central London	10 February 2023
HAT Quarter 1 Update 9.30am – 11.15am	Simon Kettlewell	Online	2 March 2023
Anti-Money Laundering – Understanding Your Responsibilities 2pm – 4pm	Rob Shaw	Online	2 March 2023
Introduction to Charities 9:30am – 4:30pm	Andrew Jarvis	Central London	10 March 2023
Introduction to the HAT Audit Methodology 9:30am – 1pm	Simon Kettlewell	Online	14 March 2023
SRA Update 10am – 12pm	Andrew Jarvis	Online	28 March 2023
Charities Update 2pm – 4pm	Andrew Jarvis	Online	28 March 2023
Introduction to SRA Assignments 9:30am – 1pm	Andrew Jarvis	Central London	18 April 2023

CAREER DEVELOPMENT COURSES

As well as a range of courses for trainees our Career Development Programme has several courses for qualified staff taking place over the next few months. In particular:

COURSE	VENUE
Becoming an Effective Supervisor	9 – 12 May 2023 - (Eastbourne)
Managers Course	19 – 21 April 2023 - (Venue TBC)
Managers Course	4 – 5 May 2022 - (Online option)

HAT RECORDED WEBINARS

In addition to the "live" CPD courses listed above, the following courses are available "on demand". A recording of the material can be provided, along with accompanying material, for attendees to watch at their leisure. For any questions or to purchase a recording please email hat@hatgroup.co.uk or speak to a member of the team.

COURSE	PRESENTER	DURATION
ISQM (UK) 1: What does it mean for me?	Andrew Jarvis	2 hours
SRA Accounts Rules Update (2022 version)	Andrew Jarvis	2 hours
AML Compliance: A guide for Senior Management (2022 version)	Andrew Jarvis	2 hours
Audit Planning Workshop	Simon Kettlewell	3 hours
Effective Audit Review	Simon Kettlewell	3 hours

Please see the HAT website www.hatgroup.co.uk for our full range of courses and further details such as pricing. Bookings can be made via our website or please email hat@hatgroup.co.uk or call 020 7213 9911 for more details.

UPDATES TO THE HAT METHODOLOGIES

The following updates have been released this year.

REFERENCE	DATE	CONTENT
TM 03/22	18 August 2022	HAT Academies Methodology – August 2022
TM 04/22	20 September 2022	HAT Corporate Audit Methodology – January 2022
TM 05/22	20 September 2022	HAT LLP Methodology – January 2022
TM 06/22	30 November 2022	HAT Compliance Pack – July 2022 (11/22 Update)
TM 07/22	23 December 2022	HAT Charities Methodology – January 2022

Our Corporate Audit and Charities methodologies dated 'January 2022' reflect the requirements of ISA 315 and ISA 240 in full.

The changes to our Corporate Audit and LLP Methodologies have now been incorporated into the CaseWare Desktop and MyWorkPapers templates.

Summaries of the changes made are freely available here.

A summary of our current methodology and compliance pack including details of effective dates can be obtained by logging into the members' area of the HAT website. Remember, key elements of our audit and non-audit methodology are available from our partners, CaseWare and MyWorkPapers. For full details of availability of our documentation within these platforms please contact us.

MAJOR PROJECTS OVER COMING MONTHS

- The final amendments are being made to specialist audit methodology to reflect the requirements of ISA (UK) 240 / 315;
- A review will be performed of the proposed amendments to FRS 102 as set out in FRED 82;
- A review will be performed of the revisions to the ICAEW / ICAS Audit Regulations to identify any amendments which may be required to the HAT Audit Regulatory and ISQM Procedures documentation; and
- The requirements of ISQM (UK) 2 and any additional amendments (for example, derived from the amendment to the Audit Regulations) will be filtered into the HAT Audit Regulatory and ISQM Procedures documentation.

TECHNICAL UPDATE

AUDITING / ETHICAL / ASSURANCE STANDARDS

FRC CONFIRMATION OF AREAS OF FOCUS IN 2023:

The Financial Reporting Council ("FRC") has announced its areas of supervisory focus for 2023 / 24, including priority sectors, for corporate reporting reviews and audit quality inspections. Its Press Release states:

"The FRC's Audit Quality Review team will pay particular attention in its audit quality inspections to areas including going concern, fraud risks, climate-related risks, and risk identification and assessment.

In selecting corporate reports and audits for review, the FRC will prioritise sectors that are under particular pressure.

Thematic reviews of corporate reporting:

The Corporate Reporting Review team will conduct four thematic reviews during the next year:

- Insurance contracts (IFRS 17): The new standard on insurance contracts will have a significant effect on corporate reporting in the insurance sector. The FRC will review a selection of insurers' 2023 interim accounts to identify compliance with IFRS 17 and examples of good disclosures;
- Large private companies: The proposed change to the definition of a Public Interest Entity will bring an enhanced regulatory focus on the largest private companies. The Government's intended threshold is entities that exceed £750 million annual revenue and 750 employees. The FRC will review a selection of private companies' annual reports to identify whether and where there are areas of poor compliance with reporting requirements with a view to informing our monitoring activities going ahead;
- Task Force on Climate-related financial Disclosures (TCFD) – metrics and targets: climate-related metrics and targets, including companies' "net zero" plans, are seen as increasingly important by investors, and the TCFD's recommendations in this area were updated in 2021; and
- Fair value measurement (IFRS 13): The FRC's review will focus on companies in the non-financial sector, and will provide an overview of the disclosure requirements of the standard, highlighting examples of better disclosure and common pitfalls.

Thematic reviews of audit:

When identifying audit thematic reviews, we have considered carefully how topics align with and complement our monitoring of the imminently effective new quality standard for firms, ISQM 1. The new standard is a more holistic and integrated standard, covering all elements of firms' systems of quality management for their audit practice and so our thematic work more naturally overlaps with this. We have selected the following topics to be covered in this inspection cycle:

- Sampling;
- Hot reviews;
- Network resources and service providers; and
- Root cause analysis.

Areas of focus for audit quality inspections:

The FRC's programme of audit quality inspections will pay particular attention to the auditor's work in the following areas:

- Going concern;
- Fraud risks;
- Climate-related risks, including the linkage between the audited financial statements and climate-related disclosures elsewhere in the Annual Report; and
- The application of the revised Auditing Standard on risk identification and assessment (ISA (UK) 315).

Other areas, including prior year areas of focus, will continue to be selected for review on individual audits applying a risk-based approach (with any financial reporting concerns identified, for example, potentially material errors in the cash flow statement, taken into account).

Priority sectors:

In selecting both corporate reports and audits for review, the FRC will give priority to the following sectors:

- Travel, Hospitality and Leisure;
- Retail and Personal Goods;
- Construction and Materials; and
- Industrial Transportation.

These sectors are considered by the FRC to be higher risk, for corporate reporting and audit, by virtue of economic or other pressures.

Given the difficult economic conditions that are currently being experienced, we recognise that many companies, in many different sectors, are currently under particular commercial and financial pressure. We will therefore be especially careful over the coming year in monitoring where these pressures are being felt most acutely, and tailor our selection of company reports for review and audits for inspection accordingly."

Although the FRC's areas of focus primarily relate to their consideration of the largest entities / audit firms, these areas of focus will be relevant to other audit regulators and therefore it is expected that there will be a similar focus by ACCA / ICAEW / ICAS during audit regulatory visits.

ACTION FOR FIRMS

Few HAT firms are directly monitored by FRC. However, the points above should be considered when preparing for monitoring visits from ACCA/ICAEW/ICAS. The above should also incorporated as appropriate into the practice-wide risk assessment required by ISQM (UK) 1 and when determining training needs for 2023.

FRC GUIDANCE ON AUDITOR SCEPTICISM AND CHALLENGE:

The FRC has published a new report setting out examples of good practice to improve auditor scepticism and challenge. The accompanying Press Release states:

"A critical attribute of an auditor's mindset and behaviour is exercising professional scepticism and challenge when performing audits. The most significant quality issues identified by the FRC over a number of years involve the inconsistent application of professional scepticism and challenge, resulting in the poor application of professional judgement.

As an improvement regulator, the report summarises what good looks like and provides examples of good practice from the FRC's ongoing supervision work."

GUIDANCE ON INTERACTION OF QUALITY MANAGEMENT AND GROUP AUDITS:

The International Auditing and Assurance Standards Board (IAASB) has published a new fact sheet on the interactions between International Standard on Audit (ISA) 220 (Revised), which addresses quality management at the engagement level, and ISA 600 on group audits. The fact sheet highlights aspects of a group audit that may be affected by ISA 220 (Revised) and International Standard on Quality Management 1 addressing quality management at the firm level. This includes the revised definition of engagement team and leadership and direction, supervision, and review responsibilities.

It highlights that the factsheet will be particularly useful for group audits in which component auditors are involved.

ACTION FOR FIRMS
All auditors working on group audits, whether as the group engagement team or as component auditors should familiarise themselves with this fact sheet.

FRC ADVISES DEFERRAL OF ARGA UNTIL 2024:

The FRC has announced its 2023-2026 draft 3-Year Plan which sets out its priorities for the next three years and the resources it will need to achieve them. Its Press Release includes:

"The plan incorporates a balanced yet assertive approach and reflects the delay of anticipated legislation to create the Audit, Reporting and Governance Authority (ARGA), which has had an impact on the associated increase in capacity, cost and headcount previously expected to occur in 2023.

The FRC has used 2022 to focus on the changes it can make with the powers it already has. The 2023-26 plan includes the completion of activities we publicised in our July Position Paper as well as looking ahead to the creation of new statutory powers and functions for ARGA, which we currently assume will occur in 2024."

ACCOUNTING STANDARDS

FRS 100 (NOVEMBER 2022):

The FRC has issued Amendments to FRS 100 Application of Financial Reporting Requirements – The Interpretation of Equivalence, which revise the Application Guidance to FRS 100 to reflect changes to company law and decisions on equivalence following the UK's exit from the European Union. The revised guidance is based on current legal requirements and is effective immediately.

The FRC has also issued a revised edition of FRS 100 Application of Financial Reporting Requirements. This revised edition incorporates the revised Application Guidance and other amendments made since the previous edition was issued in 2018, as well as changes in Irish company law.

AMENDMENTS TO UK-ADOPTED INTERNATIONAL ACCOUNTING STANDARDS:

The UK Endorsement Board ("UKEB") adopted three narrow-scope amendments, which were published by the IASB in 2021 as follows:

- Disclosure of Accounting Policies (Amendments to IAS 1 Presentation of Financial Statements and to IFRS Practice Statement 2 Making Materiality Judgements);
- Definition of Accounting Estimates (Amendments to IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors); and
- Deferred Tax related to Assets and Liabilities arising from a Single Transaction (Amendments to IAS 12 Income Taxes).

These amendments are effective for annual periods beginning on or after 1 January 2023, with early application permitted.

The UK-adopted international accounting standard text for these amendments can be found here.

PERIODIC REVIEW OF FRS 102:

The FRC has issued Draft amendments to FRS 102 The Financial reporting Standard applicable in the UK and Republic of Ireland and other FRSs – Periodic Review. Their Press Release states:

"FRED 82 proposes a number of changes resulting from the second periodic review of FRS 102 and other Financial Reporting Standards. The proposals include: a new model of revenue recognition in FRS 102 and FRS 105; a new model of lease accounting in FRS 102; and various other incremental improvements and clarifications. The FRED is accompanied by a consultation stage impact assessment.

In developing FRED 82, the FRC has considered changes to IFRS Accounting Standards, the IASB's proposed changes in developing the third edition of the IFRS for SMEs Accounting Standard, stakeholder feedback in response to the FRC's 2021 request for views, and other developments in corporate reporting.

As a result of the amendments set out in FRED 82, FRS 102 will reflect up-to-date IFRS-based solutions, providing high-quality and clear financial reporting to users. This will include more transparent reporting of lease obligations, as well as a clear five-step model for determining the recognition of revenue from all contracts with customers. The proposals have been designed to be proportionate to the size and complexity of the entities applying the standards.

The proposed effective date of the amendments set out in the FRED is 1 January 2025. Comments on FRED 82, including the consultation stage impact assessment, are requested by 30 April 2023."

As is noted above, it is proposed that there are amendments to how revenue and leases are recognised, in order to follow the requirements of IFRS 15 / IFRS 16. HAT will keep firms up to date regarding these requirements and in due course will set aside time to reflect these amendments within HAT documentation.

HAT RESPONSE
These proposals, if implemented will have a significant impact on all firms. HAT will provide an overview of these proposals in our Q1 Accountancy and Audit Update and will also formally respond to the consultation paper on behalf of firms.

FRC ADVICE ON WHAT MAKES A GOOD ANNUAL REPORT:

The FRC has published 'What makes a Good Annual Report and Accounts', which sets out the attributes for a high-quality Annual Report and Accounts (ARA). Their Press Release states:

"The ARA is the cornerstone of corporate reporting and should provide investors and other stakeholders with clear and relevant information on the company's performance and prospects to help them make informed investment decisions and to promote effective stewardship.

As an Improvement Regulator, the FRC uses a principles-based framework which identifies corporate reporting principles and effective communication characteristics.

To Illustrate these, today's publication provides a range of good practice examples which have been identified by the FRC as part of our ongoing supervision work.

A high-quality ARA will:

- Comply with relevant accounting standards, laws and regulations, and codes;
- Be responsive to the needs of stakeholders in an accessible way; and
- Demonstrate the corporate reporting principles and effective communication characteristics outlined in this publication."

ANTI-MONEY LAUNDERING

AMENDMENT TO HIGH RISK THIRD COUNTRIES:

The recent FATF Plenary amended jurisdictions under increased monitoring, such that new jurisdictions subject to increased monitoring are the Democratic Republic of Congo (DRC), Mozambique and Tanzania, with Nicaragua and Pakistan no longer being subject to increased monitoring.

This has resulted in UK legislation being amended to reflect a new list of High Rick Third Countries, with The Money Laundering and Terrorist Financing (High-Risk Countries) (Amendment) (No. 3) Regulations 2022 (SI 2022 / 1183), which came into force on 15 November 2022, reflecting this amendment.

Separately, HM Treasury has updated guidance on applying enhanced due diligence in respect of a relationship with an individual / entity with links to a high risk third country. In particular, this says:

"While regulation 33(3A) of the MLRs is clear through sub-paragraphs (a)-(f) about what steps must be taken, relevant persons should consider the intensity with which they undertake these steps (i.e., the level of detail, the type of verification) in order to meet their obligations. Within the constraints of regulation 33(3A), relevant persons can take a risk-based approach when applying EDD to existing customers. For example, by prioritising higher-risk customer groups, or considering the level of information gathered. The level of enhanced customer due diligence and enhanced ongoing monitoring undertaken should be proportionate to the level of risk attributed to the customer. This will differ between institutions, and between customers depending on other risk factors present. Relevant persons should consider factors such as the specific shortcomings mentioned by the FATF, and the risk typologies most relevant to the jurisdiction in question. Regulated persons should refer to their sector-specific guidance, approved by HM Treasury, for further advice on meeting their obligations under regulation 33."

ACTION FOR FIRMS
You must ensure the current list of high-risk jurisdictions is available to all team members and considered when updating client due diligence documentation. Where clients are in a high-risk jurisdiction, the additional guidance from HM Treasury should be considered.

BAN ON AUDITING SERVICES WHEN THERE ARE RUSSIAN-LINKED CLIENTS:

The Russia (Sanctions) (EU Exit) (Amendment) (No. 17) Regulations 2022 (SI 2022 / 1331) ("Amendment 17") have been laid before Parliament and these came into force on 16 December 2022. These amend The Russia (Sanctions) (EU Exit) Regulations 2019 (SI 2019 / 855) ("the Regulations")

The primary amendment which has relevance for accounting / auditing firms is for Reg. 54C of the Regulations to be amended by Reg. 10 of Amendment 17 such that it now reads (in terms of prohibited professional and business services):

a. accounting services;
b. advertising services;
c. architectural services;
d. auditing services;
e. business and management consulting services;
f. engineering services;
g. IT consultancy and design services; or
h. public relations services.

In addition, Reg. 14 of Amendment 17 amends the exceptions relating to the provision of professional and business services (Reg. 60 DA of the Regulations) and in respect of the provision of accounting services, this now reads:

1. The prohibitions in regulation 54C (professional and business services), in so far as they relate to accounting services, business and management consulting services, engineering services or public relations services, are not contravened by any act done by a person ("P") in satisfaction of an obligation in respect of the provision of those services by P to a person connected with Russia where the services are provided in relation to the discharge of or compliance with UK statutory or regulatory obligations, such obligations not arising under contract.

In respect of auditing services, this now reads:

3. The prohibitions in regulation 54C, in so far as they relate to auditing services, are not contravened by any act done by a person ("P") in satisfaction of an obligation arising from the appointment of P as the auditor of a parent undertaking ("C") provided that:
    a. where C is a credit institution, the auditing services of P are for one or both of the purposes mentioned in paragraph (4);
    b. where C is not a credit institution, or is a credit institution that does not meet the condition in sub-paragraph (a):
        i. P is appointed as auditor of C before 16th December 2022,
        ii. the act is carried out before the end of 31st May 2023, and
        iii. P notifies the Secretary of State of the provision of the services, before or after the act is carried out, by the end of 15th March 2023.
4. The purposes are -
    a. C, in its capacity as a parent undertaking, deciding whether accounts of a subsidiary undertaking of C which is a person connected with Russia ("S") should be included in consolidated group accounts of C, and
    b. the inclusion in consolidated group accounts of C of the accounts of S.
5. The prohibitions in regulation 54C, in so far as they relate to auditing services, are not contravened by any act done by a person ("P"):
    a. in satisfaction of an obligation arising from the appointment of P as the auditor of a subsidiary undertaking ("S") in respect of the provision of those services to S in relation to the discharge of or compliance with UK statutory or regulatory obligations, and
    b. which results in the provision of those services indirectly to a person connected with Russia in that person's capacity as a parent undertaking of S.

Further information regarding this is also available from the ICAEW website.

ACTION FOR FIRMS
Where it is intended to rely upon one of the revised exceptions noted above, it is advisable for legal advice to be sought prior to continuing to provide accounting and / or auditing services.

ICAEW / ACCA / REGULATORY

AMENDMENT TO ICAEW / ICAS AUDIT REGULATIONS:

ICAEW have published updated Audit Regulations which apply to firms regulated by ICAEW / ICAS / ICAI for the conduct of audit work in the United Kingdom. These apply from 5 December 2022 and are accompanied by a summary of changes, which highlights the following:

"The changes made can be summarised as:

- The registration regulations have been modified to recognise the additional registration process now required by the FRC in respect of firms that carry out the audits of Public Interest Entities (PIEs);
- The rules around ownership and control of firms have been clarified to address some of the issues arising from complex firm structures and Brexit legislation;
- The period allowed for the exercise of dispensations has been clarified;
- The replacement of ISQC 1 by ISQM 1 for quality management; and
- Some terminology has been amended to reflect changes in the disciplinary framework."

PIE AUDITOR REGISTRATION:

The FRC has issued a reminder that from 5 December 2022, all audit firms and responsible individuals (RIs) who undertake statutory audit work for Public Interest Entities (PIEs) must be registered by the FRC.

By directly registering audit firms and individuals signing PIE audit reports, the FRC can act decisively when it identifies systemic issues that risk affecting audit quality.

This enhances the FRC's ability to drive improvements, ensure firms are growing sustainably and more closely monitor the auditor's work as well as enabling the FRC to apply conditions or undertakings when concerns are identified.

To date, 39 audit firms and around 650 RIs have been registered and are included on the PIE Auditor Register.

ACTION FOR FIRMS
Remember you can no longer act as an auditor of a PIE entity without first registering with the FRC for this purpose.

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