Understanding the BEIS consultation

‘Restoring trust in audit and corporate governance’

A series of frequently asked questions on the key proposals

Increased director and audit committee accountability and reporting responsibilities

Introduction

On 18 March 2021, the Government (BEIS) published its long-awaited consultation on reforms aimed at ‘Restoring trust in audit and corporate governance’ (the Consultation). It’s a significant consultation with 98 questions covering almost all 155 recommendations from the Kingman, CMA and Brydon reviews, and sets out a broad programme of reform for auditors, companies, directors, audit committees, investors, other stakeholders and the regulator. The deadline for responses to the Consultation was 8 July 2021. See our summary briefing document for more details of the key proposals.

These ‘frequently asked questions’ are part of a series intended to help you understand the implications of these proposals in more detail.

This is not an exhaustive list, and we’re sure there will be plenty of questions we’ve not yet considered.

Our answers are based on our interpretation of the Government’s proposals. There’s also still a lot of uncertainty about what will be implemented, and the details of any new regime; the thoughts we’ve set out below are designed to help you consider the implications for your organisation, but please do remember that the final rules could well result in a different outcome.

A number of the proposals seek to increase director and audit committee accountability and reporting responsibilities. These proposals could have a significant impact on executive and non-executive directors. Here we’ve answered questions over what these proposals entail and what they could mean in practice.

If you would like to discuss any of these points further, please ask your usual PwC contact, or alternatively you can contact:

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Background

1 Why does the Government think directors need to be held more accountable?

In the Consultation the Government stresses that it is vital that directors of the largest companies are held to account, both to protect the interests of shareholders and because a loss of trust in directors and companies could have far-reaching adverse effects across the UK. As described below, today there's a rather complex picture when it comes to holding directors accountable; the Government believes one of the consequences of this complexity is that if there are instances of poor or misleading corporate reporting – or weak internal controls that lead to errors in reporting – it's actually quite hard for directors to be held to account. That was the conclusion reached by Sir John Kingman when he undertook his independent review of the FRC – and he recommended to the Government that there needed to be a clearer and simpler accountability regime for directors in respect of their corporate reporting and audit responsibilities.

2 What is the current regime for directors' accountability as it applies to accounting and reporting?

Today directors face a patchwork of responsibility and accountability regimes in relation to corporate reporting and audit. There are directors' duties under the Companies Act, duties under the Listing Rules and other FCA regulations and of course the current regulator, the FRC, owns the UK Corporate Governance Code (the Code) which sets out principles to be followed by directors of premium listed companies. Here is a summary of the various elements:

Companies Act – The Companies Act 2006 includes directors' duties in respect of:

- **Company accounts and reports:** Directors have a duty to keep adequate accounting records and to prepare reports (e.g. strategic, remuneration and directors' report) which need to be approved by the board of directors and signed off by a director on behalf of the company.
- **Audit:** Directors have the duty to appoint an auditor and provide information or explanations at the request of the auditor.

Listing rules – Directors of companies that are listed in the UK (whether incorporated in the UK or elsewhere) must follow minimum requirements for the admission of securities to listing, the content, scrutiny and publication of listing particulars, and continuing obligations of companies after admission. For example, directors of a company that is seeking a premium listing of its shares on the Main Market of the London Stock Exchange, have to be satisfied that there are established procedures that provide a reasonable basis for them to make proper judgements on an ongoing basis as to the financial position and prospects (FPP) of the applicant and its group (Listing Rule 8.4.2(4)).

UK Corporate Governance Code

The Code applies to companies that have a premium listing in the UK (whether incorporated in the UK or elsewhere), and contains Principles, Provisions and guidance. Whilst the Principles must be adopted, the Provisions apply on a 'comply or explain' basis.

Section 4 of the Code sets out the requirements relating to audit, risk and internal control and sets out both Principles and Provisions that relate to accounting and financial reporting. Principle M provides that 'The board should establish formal and transparent policies and procedures to ensure the independence and effectiveness of internal and external audit functions and satisfy itself on the integrity of financial and narrative statements' and Principle N provides that 'The board should present a fair, balanced and understandable assessment of the company's position and prospects'. The Provisions include requirements for the board relating to: establishing an audit committee and setting out its main roles and responsibilities; stating in annual and half yearly statements whether it considers it appropriate to adopt the going concern basis of accounting and to identify any material uncertainties to the company's ability to do so over at least the next 12 month period. Directors should also explain their responsibility for preparing the annual report and accounts and state that they consider the annual report and accounts, taken as a whole, is fair, balanced and understandable, and provides the information necessary for shareholders to assess the company's position, performance, business model and strategy. The board should also confirm that it has assessed the prospects of the company and whether it has a reasonable expectation that the company will be able to continue in operation and meet its liabilities.

The Listing Rules require that companies report on how they have complied with the Code in their annual report; clear explanations are expected if a company has departed from any of the Provisions. The Code does not create any additional director duties in itself.

FCA – Of course, directors of financial services companies face additional responsibilities, for example, those set out by the FCA:

- **FCA Handbook:** Companies (and company directors) in the financial services industry are subject to the Principles and Code of Conduct set out in the FCA Handbook. There are 11 Principles which include requirements to: conduct business with integrity, due skill, care and diligence; observing proper standards of market conduct; take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems.

- **Senior Managers and Certification Regime (SM&CR):** Individuals who perform a senior management function (at an FCA solo regulated company) must be approved by the FCA and produce a statement of responsibilities that sets out what they are responsible and accountable for, there are also prescribed responsibilities set out in the FCA Handbook that will apply. Each senior manager is subject to a statutory 'duty of responsibility' which means if something goes wrong in an area that they are responsible for, the FCA will consider whether they took reasonable steps to stop this from happening and can take action if a breach has occurred. This regime is applicable to directors performing a senior management function, regardless of whether they are UK based or overseas.

3 In what ways are directors held accountable today if they breach their duties/responsibilities?

In theory, shareholders could bring an action for breach of duties under the Companies Act against a director; in fact they have to get the Court's permission to do that, and then the company itself would have to take action against the director. This means it is a complicated process and rarely happens.

The FCA can pursue directors for breaches of FCA regulations, including the Listing Rules, – but in practice (at least outside of financial services) that's very rare, and typically only happens for truly egregious offences like insider trading.

The Code has no enforcement mechanism attached to it at all; the theory is that the company's shareholders should exert pressure on the directors to change their behaviour in the event of non-compliance.

If there's an error in the accounts, the FRC has rights of enforcement, but the FRC can only pursue a director if s/he happens to be a member of a professional accounting or actuarial body. In addition, the FRC's regulatory locus extends only over the financial statements and certain sections of the 'front half' of the annual report and not over the whole annual report.

The Insolvency Service has powers to investigate directors – and ultimately could order that a director be disqualified. That is a power that's used, but the Insolvency Service has limited resources and so it tends to use this power only in very high profile situations.

Increased accountability of directors

4 What is being proposed by the Government and will it apply to all directors?

The core proposal from the Government is that the new regulator, the Audit, Reporting and Governance Authority (ARGA) would have the power to investigate and sanction breaches of corporate reporting and audit-related responsibilities by directors of public interest entities (PIEs).

There's a few critical elements of this proposal:

- Firstly, it applies to directors of PIEs. Currently PIEs comprise Main Market listed companies, banks and insurance companies. But the Government has a separate proposal to expand the definition of a PIE to include large AIM listed companies, large private companies (including those owned by overseas entities) and perhaps even large charities. Refer to our previously issued FAQs on the proposal to expand the PIE definition.
- Secondly, it applies to ALL directors. This moves beyond today's position where only directors who are members of professional bodies can be held to account by the FRC and puts all directors, even non-executive directors, at risk of enforcement. Interestingly, Sir John Kingman recommended in his review that the focus of enforcement should be on the Chairman, the CEO, the CFO and the audit committee chair, but the Government proposes moving beyond that to a regime where all directors could be held to account.
- Thirdly, the proposal is concerned with **breaches** of 'corporate reporting and audit related responsibilities'. This takes the bar for enforcement action down to what could be quite a detailed level; potentially it's a lot easier to breach a corporate reporting responsibility than it is to be negligent in following directors' duties. It's important to note also that the Consultation proposes lots of new corporate reporting responsibilities, including the potential for a strengthened UK internal control regime (so-called UK SOx). These new reporting responsibilities are discussed further in questions 10 to 27 below.

5 What would happen if the regulator was to exercise these powers?

The Consultation tells us that ARGA would have power to gather information from a company and its directors and carry out an investigation in order to determine whether rules have been breached. Ultimately ARGA could impose a graduated range of civil sanctions, which could include reprimands, fines and, in the most serious cases, temporary prohibitions on acting as a director.

The Consultation also acknowledges that many of the existing statutory duties for corporate reporting and auditing are not designed for enforcement by a regulator. A good example of this is the Companies Act requirement to maintain 'adequate accounting records', as no-one has ever explained, or tested, what that actually means in practice. So in the Consultation, ARGA is also being asked to set out more detailed requirements as to how certain statutory duties relating to corporate reporting should be met by directors. Interestingly, this exercise would also include ARGA considering some of the more behavioural standards, such as the duties to exercise independent judgement and reasonable skill, care and attention.

This would all appear to signal a big change for directors and a huge responsibility for the new regulator, first of all in setting standards for directors that are clear and proportionate, and then in exercising its ability to supervise the application of those standards, and to enforce where there are breaches, in a fair and transparent manner.

Increased scrutiny of audit committees

6 There is a proposal for increased scrutiny of audit committees over audit tendering and monitoring of the audit. Why is the Government making this recommendation?

Both the review of the audit sector by the Competition and Markets Authority (CMA) and Sir John Kingman's review of the FRC raised concerns that the commercial relationship between a company's audit committee and its chosen auditor could result in a lack of scepticism being exercised by both parties. The CMA also commented that 'cultural fit' and 'chemistry' played a part in the selection of auditors by audit committees. As a result, the CMA recommended that audit committees should be required to meet minimum standards and come under greater scrutiny by ARGA in relation to audit tender processes and the ongoing monitoring of the audit.

In our experience, many audit committees already function to a high standard, however, an enhanced regulatory framework and increased reporting and oversight could be useful in bringing greater consistency between audit committees.

7 What are the current requirements of audit committees when it comes to the audit tender process and the audit?

Most PIEs are required to establish an audit committee (or body performing equivalent functions). The audit committee is there to act as a safeguard in protecting the interests of shareholders in relation to the company's external audit. In choosing an audit firm, the audit committee must carry out a prescribed selection process (under the Companies Act 2006) after which it must make a recommendation to the board of its first and second choice candidates for auditors, together with reasons for those choices. The tender documents must contain non-discriminatory clauses and the audit committee must make a statement confirming that the recommendation is free from third party influence, and that there are no contracts restricting the choice of auditors. The audit committee also has a number of other ongoing functions in relation to the audit, including: reviewing and monitoring the auditor's independence and objectivity; reviewing the effectiveness of the audit; and informing the board as to the outcome of the audit.

8 What is being proposed by the Government for audit committees?

The Government is proposing that a new regulatory framework be created whereby ARGA imposes additional requirements on audit committees in relation to the appointment and oversight of auditors. Exact details of the requirements are not covered by the Consultation, but it does say that they would cover the need for audit committees to monitor audit quality continuously and consistently demand challenge and scepticism from auditors. These requirements would take the form of minimum standards, set by ARGA, that would still allow audit committees to exercise discretion and professional judgement (and also to exceed the standards if they wished).

ARGA would have a duty to monitor compliance with the new requirements, the power to require information and/or reports from audit committees and the power to place an observer on the committee if there were concerns about compliance. It's not clear from the Consultation what form this 'monitoring' would take, but we can see in the Government's Impact Assessment that accompanies the Consultation that the Government is assuming that each year ARGA would perform targeted monitoring of five audit tenders and of the ongoing activities of 50 audit committees. ARGA would also have the power to take action against the audit committee if they were deemed to have breached the new requirements. This could include issuing a public reprimand or the commissioning of a skilled person review.

It is worth noting that in the Impact Assessment it is assumed that audit committees are already largely complying with the FRC's guidance for audit committees and so would not need to collect and collate new information to meet any new requirements, but might need to repackage the information they already have. In our experience, most audit committees embrace the spirit of the existing regimes, but the documentation and evidence they retain to support their compliance is variable.

9 Which companies would the minimum standards for audit committees apply to?

This proposal is focussed on audit committees of FTSE 350 companies, with the Government commenting that an extension to all PIEs could be considered 'in due course'. In the Impact Assessment, we see that the Government is assuming that all FTSE 350 companies would be required to adhere to the minimum standards, but that those deemed to be 'high risk' would also need to report to the regulator on their tendering, oversight and management of the audit. The definition of 'high risk' could perhaps be aligned to the FRC's existing AQR risk assessment framework for selecting companies to inspect.

As noted in question 8, we can also see in the Impact Assessment that the Government is assuming that five tenders a year (14% of an estimated total 35 tenders) and 50 ongoing audits a year would be subject to risk-based monitoring by ARGA; this is said to be in line with the average sample size for the FRCs Audit Quality Review programme.

New reporting responsibilities for directors

10 What are the new reporting responsibilities for directors and which companies would these apply to?

There are a number of new reporting responsibilities for directors which involve new 'statements' or disclosures in the financial statements or the 'front half' of annual reports. We believe that it's reasonable to assume that these responsibilities would fall under the new regulatory enforcement regime for directors, discussed above:

- **A strengthened regime for internal controls over financial reporting (ICFR) –** Directors of premium listed companies, followed by all PIEs after two years, would make an explicit statement about the effectiveness of ICFR, explaining how they had carried out their assessment, details of the outcome (with any deficiencies), the benchmark system used to make the assessment and how they had assured themselves it is appropriate to make the statement. ARGA would also have the power to investigate the accuracy and completeness of the directors' internal controls disclosures and have the power to sanction directors where they have failed to establish and maintain an adequate internal control structure and procedures for financial reporting. For more detail on this proposal please see our previously issued FAQs
- **Dividend and capital maintenance disclosures**
- **More transparency around resilience planning**
- **The steps taken to prevent and detect material fraud**
- **Supplier payment practices**
- **Audit and assurance policy**
- **Sharing the annual audit plan**

Below, we've answered some of the more frequently asked questions about these last six new reporting responsibilities.

Dividend and capital maintenance disclosures

11 What is being proposed?

Following a number of high profile examples of companies paying out significant dividends shortly before profit warnings and, in some cases, insolvency, it is proposed that listed companies (on the London Stock Exchange and AIM), with a possible future extension to all PIEs, disclose their distributable reserves and an estimate of the group's dividend paying capacity. There is also a recommendation that the directors make a statement about the legality of proposed dividends and the effects on future solvency.

12 Where in the annual report would the new disclosures be presented and will they be subject to audit?

It's clear in the Consultation that the company disclosure of distributable reserves (in the case of a group – the parent company) and the disclosure of the group's dividend paying capacity would need to be included in the financial statements of the parent company and, as such, would be subject to audit.

However the Consultation is less clear about where a directors' statement on the legality of proposed dividends and the effects on future solvency would be housed – whether in the annual report or elsewhere. Given the link with the Resilience Statement (see question 18 below for more details) and s172(1) statement, as well as the existing disclosure of proposed dividends in the directors' report, we believe that it would be sensible for this to be a 'front half' disclosure in the annual report, possibly as an extension of the disclosure of proposed dividends. Locating the statement here would mean that it would not be audited; instead the statement would be covered by the requirement for the auditor to read the disclosures and consider whether there are any material inconsistencies with the financial statements or their knowledge from the audit. If the company were to decide that further assurance over the statement was desirable, this could be considered as part of the Audit and Assurance Policy described in question 25 below.

13 What if it is not possible to determine the exact amount of my company's distributable reserves?

The Consultation acknowledges that there may be situations where it is impossible to calculate the distributable reserves figure exactly, for example when a company's profit history goes back many years. In this situation, companies would be permitted to report a 'not less than' figure for distributable reserves. This would act as a 'dividend cap' and any proposed dividend would not be allowed to exceed this known figure.

14 Will there be guidance over how to present the group's dividend paying capacity?

The Government expects the new regulator (ARGA) to consider issuing guidance to companies on how to comply with this requirement, but also notes that there could be a degree of discretion and flexibility that allows parent companies to select which group companies to include in the assessment.

In our view, this disclosure has the potential to be complicated and problematic. In groups where there are many large overseas subsidiaries subject to different legal regimes for paying dividends it could be difficult to determine how associated reserves should be reflected in the proposed disclosure of the group's dividend paying capacity. There will also need to be guidance on how the various assumptions on the consequences of intra-group distributions for asset carrying values and, potentially, future investment opportunities would need to be disclosed.

15 What is the statement about the legality of proposed dividends and the effect on future solvency intended to achieve?

The statements on distributable reserves are valuable although they are largely backward looking; they do not consider any future cash demands which the business could face, or other such threats to future solvency. The proposal to require directors to make a statement about the legality of proposed dividends and the effect on future solvency would require a forward looking approach. Amongst other things, the directors would need to confirm that it is their reasonable expectation that payment of the dividend would not threaten the solvency of the company over the next two years in light of the risk analysis undertaken and the directors' knowledge of the company's position at the date the dividend is proposed. They would also confirm, 'where relevant', that the dividend is consistent with the Resilience Statement. Here we think it will be important for ARGA to consider how this statement relates to the proposal for a Resilience Statement which currently does not contemplate a two year look-forward period.

16 This all sounds like quite a time consuming and costly process, particularly if companies have to produce 'auditable' disclosures. How much is it going to cost?

In the Impact Assessment, the Government assumes that companies will already have a lot of the information required for the disclosures readily available to them but acknowledges that there could be significant variations between companies in the need for additional work. In our experience, there can be much variability in companies' historical records of profits; we believe therefore that the Government may have underestimated the costs of compiling these new disclosures, in particular in the first year.

Furthermore, as we note above, we expect that compiling and auditing the group-wide disclosure of dividend paying capacity could be very complicated for large global companies. We expect that this could involve significant time and effort, both in the first year and on an ongoing basis.

More transparency around resilience planning

17 What is being proposed?

The Consultation has proposed that premium listed companies, with an extension to all PIEs after two years, would produce a 'Resilience Statement' that, effectively, would combine the existing going concern statement and viability statement into one statement. The new statement would address business resilience:

- over the short term (incorporating the company's existing going concern statement);
- the medium term (incorporating the current viability statement requirements, albeit with better scenario planning disclosures and over a longer period of five years); and
- the long term.

Notably, there is a recommendation that potential material uncertainties be disclosed that were considered by management in their going concern assessment, even if they were subsequently determined not to be material after the use of significant judgement and/or the introduction of mitigating action. Also, the Government has proposed that at least two reverse stress tests should be included within the medium term part of the statement.

18 How is the proposed Resilience Statement different to the viability statement we have today?

Other than the inclusion of the going concern statement, the concept of the Resilience Statement has a similar objective to that of today's viability statement – to demonstrate to shareholders and wider stakeholders how companies are building business resilience to cope with severe but plausible scenarios in the short and medium term. However, as the Government notes in the Consultation, whilst existing risk and viability reporting requirements produce useful disclosures, the viability statement in particular has not proved as effective as originally hoped, with a lack of detail on risk scenario planning and an almost 'default' assessment period of three years.

Medium term reporting would include information on the company's approach to capital maintenance and wider financing, including how it is balancing dividends and other distributions with the company's liquidity needs. As we note in question 12 above, it is proposed that the directors would make a statement on the legality of proposed dividends and the effects on the future solvency of the company over the next two years. As part of this dividend statement, the directors would confirm that the dividend is consistent with the Resilience Statement. It will be important for ARGA to consider how these two statements fit together, as the two-year look forward period included in the requirements for the dividend statement is not contemplated here.

Also in the medium term part of the assessment, the Government is proposing that at least two reverse stress tests be included (see question 19 below).

There is a question in the Consultation over whether the long term reporting in the Resilience Statement would include consideration of the company's climate related disclosures (see question 20 below).

In terms of time periods, the Government is proposing that the medium term period should be required to be five years. There is also a specific question in the Consultation about whether other specific disclosure should be included, for example, supply chain resilience and other areas of significant business dependency; digital security risks; and climate change risk.

19 What are the reverse stress tests the Goverment proposes would be required?

Stress testing is a forward-looking analysis technique that many entities already carry out to some degree, if not in name. An entity identifies an appropriate range of adverse scenarios of varying nature, severity and duration relevant to its business, and considers its exposure to those scenarios. A reverse stress test is a stress test that starts from the opposite end – with the identification of a pre-defined outcome. This might be the point at which an entity can be considered as failing, or the entity's business model becomes unviable. Severe but plausible scenarios that might result in this outcome are then explored.

The Government is proposing that companies would disclose at least two reverse stress tests. In our view, where there are distinct scenarios which could give rise to business model failure, we agree with the Government that it will be helpful for companies to tackle each scenario separately in the Resilience Statement. For companies with a very simple business model we hope that the implementation guidance will allow proportionate disclosure.

The Government also says in the Impact Assessment that they expect stress tests to present significant challenges to in-scope companies, especially for the first and second years of implementation, and that companies could therefore face significant costs from this requirement.

20 How might climate-related risks be considered as part of the Resilience Statement?

The Government suggests that the long-term part of the Resilience Statement could be a means for companies to provide disclosures consistent with the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). We are aware that the TCFD is keen to see reporting against its framework being integrated into the annual report and this would be consistent with that approach.

Wherever the TCFD disclosures are located in the annual report we believe that it would make sense to integrate them with the overall narrative on risks and resilience.

If they are to be included in the Resilience Statement, we think care will be needed to make sure that TCFD disclosures do not 'overwhelm' other, equally important, areas of the Resilience Statement or, conversely, get lost within the other Resilience Statement disclosures.

The steps taken to prevent and detect material fraud

21 What is being proposed?

The Government is proposing that directors of PIEs report on the steps they have taken to prevent and detect material fraud. The Government believes this will reinforce directors' primary responsibility for fraud prevention and detection and may also, in some cases, enhance their focus on the risks relating to fraudulent financial reporting.

22 Is there any indication in the Consultation as to what this disclosure would look like?

There's not a lot of detail in the Consultation about what the directors' disclosure will look like in practice. However, there is an indication in the Impact Assessment, which states that the directors would be required to report on the actions they have taken to fulfil their obligation to prevent and detect material fraud. It goes on to say that such actions may include undertaking an appropriate fraud risk assessment and responding appropriately to identified risks; promoting an appropriate corporate culture and corporate values; and ensuring appropriate controls are in place and operating effectively.

It also states that although directors would be required to report on the actions taken to prevent and detect fraud, they would not be expected to take any additional action to prevent and detect fraud (although some may choose to do so if they felt their current work was insufficient).

Therefore, the Government expects costs to arise only from the preparation of the statement, which, in the main, would involve the repackaging of existing information. They expect these costs, and the additional costs expected from the increased auditor responsibility (refer to question 23 below), to be negligible.

Based on this additional detail in the Impact Assessment, we would assume, at a minimum, companies would need to prepare a fraud risk assessment to support their disclosure. Directors might also consider testing internal controls relating to fraud – it's possible that this could become a requirement as part of the strengthened UK regime over internal controls. In our experience, there is much variability in the rigour of companies' existing fraud risk assessments, with many companies not yet having a formal process in place.

23 Would the auditor have increased responsibilities for reporting about the risk of fraud?

As outlined in question 21 above, the Government is proposing that the directors of PIEs make a statement about the steps they have taken to prevent and detect material fraud. The Government's proposal also includes a requirement that the auditors report on the work they have performed to conclude whether the directors' statement is 'factually accurate'. Separately, auditors would then report on the steps they themselves had taken to detect material fraud and assess the effectiveness of 'relevant controls' – which we assume refers to the controls the company has in place to prevent and detect material fraud.

Both of these requirements would place new responsibilities on the auditor compared with today's regime. In particular, in today's audits of financial statements it would not be routine for an auditor to assess the effectiveness of controls in place to prevent and detect material fraud.

If the directors choose to commission assurance on their statement in respect of ICFR from the statutory auditor, it's possible that this assurance work may overlap with the auditor's assessment of fraud controls. If not, we expect that this new requirement will create incremental work for financial statements auditors.

Supplier payment practices

24 What is being proposed?

Directors of PIEs would disclose a summary of how the company, or group (in the case of a parent company) has performed with regard to supplier payments over the previous reporting year.

25 What is being proposed?

The Government is proposing a statutory requirement for audit committees/boards, initially of premium listed companies, with a possible extension to all PIEs in the future, to develop an Audit and Assurance Policy (the Policy) to be put to shareholder advisory vote. The Policy would explain what independent assurance the company intends to obtain in the next three years in relation to the annual report and other company disclosures (much of this information is not currently covered by the audit of the financial statements). The policy would explicitly describe what, if any, independent assurance is planned in relation to:

- the new Resilience Statement, in whole or part, and other disclosures related to risk; and
- the effectiveness of the company's internal controls framework.

(We note this second bullet appears to require that the directors explain their approach to obtaining independent assurance over the entire internal controls framework and is not just limited to the internal controls around financial reporting, which is where the directors statement described in question 10 above is focused.)

Other required elements of the Policy would include:

- a description of the company's internal auditing and assurance processes, perhaps describing how management's conclusions and judgements in the annual report and accounts can be challenged and verified internally. This could be a change in focus for some internal audit functions as often the focus is on the operational aspects of a business rather than the financial statements;
- details of the policies the company has in relation to tendering external audit services; and
- whether and how the company had taken into account shareholder and employee views in formulating the policy.

This last bullet is interesting to note as it introduces employee involvement for the first time in the Consultation.

26 How often would the Policy be published and where will it be disclosed?

The Government's preferred option (although they are open to comments) is that the policy is prepared and published annually, but covering a three-year rolling outlook. Listed companies would have their policy voted on annually.

It is not defined in the Consultation where the Policy would be disclosed. It is possible it could be published in the front half of the annual report. However, it is more likely it will be a separate section on the company's external website.

Sharing the annual audit plan

27 What is being proposed and how is that similar or different to the Audit and Assurance Policy?

In addition to the Audit and Assurance Policy, the Government is suggesting that a mechanism be established to require audit committees of premium listed companies, with possible expansion to other PIEs in the future, to gather shareholder views on the statutory auditor's annual audit plan. At the start of every audit cycle there are a number of matters that the auditor is required to communicate to a company's audit committee in relation to the audit. These include the auditor's consideration of key risks and their scoping and materiality decisions. This communication often takes the form of an 'audit plan' which is agreed with the audit committee (or equivalent) before the formal audit work begins.

The Government believes that shareholders could benefit from seeing a summary version of the audit plan that has been provided to the audit committee (subject to necessary safeguards on the publication of commercially sensitive information); shareholders would be free to share suggestions for amendments to the audit plan to reflect their own views of areas of increased audit risk. The Government is clear, however, that any shareholder views on the plan should be purely advisory in nature to ensure that the auditor retains autonomy for the way the audit is conducted. It's also noted that while a wide range of risks affecting the audited entity will be of interest to shareholders, the auditor should not be required to consider proposals which fall outside of the scope of the statutory audit.

The audit committee's annual report would set out which shareholder suggestions put forward for consideration had been accepted or rejected by the auditor.

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