UK Finance response to the FRC call for feedback on the Providing Assurance on Client Assets standards

Introduction

UK Finance commends the FRC for its work on its standard on Providing Assurance on Client Assets to the Financial Conduct Authority (to be referred to in this response as “the standards”). The standards have had a broadly positive impact on the quality of the audit work, providing a clear framework to the auditors, who typically use the standards as an anchor to derive their own interpretation of the Client Asset (CASS) rules, and their own expectations on how the related issues should be approached.

The standards have also been of significant benefit to firms, providing them with greater visibility as to the process behind audit requirements, a clearer view of CASS applicability, controls and risks, and the general need to meet the FRC standards. However, despite the best efforts of firms, auditors, and other related stakeholders, we have observed that an improved framework has not necessarily resulted in better quality audits in all cases.

UK Finance has included in this response an appendix which provides comments as to how the FRC can further develop the standards. We would be pleased to have the opportunity to discuss our recommendations with the FRC in due course.

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Appendix

(i) Auditors expertise

UK Finance concerned that audit firms do not always have the technical expertise and understanding to perform audits to prescribed levels. Audit teams are often auditing on what might be considered a “mechanical process”, as opposed to truly understanding the CASS risks involved in what they audit. A potential reason for such an approach is a “fear factor” in making judgement calls on technical matters. We would caveat this comment by stating this is not always the case, and it may be a challenge that to some extent is beyond the FRC’s control, but it is an issue that can negatively impact the auditing process, and we ask the FRC to give some thought to the issue.

(ii) Consistency of auditing

UK Finance believes auditors should provide greater justification as to their rationale on areas where they take a position beyond the written scope or intent of the rules, and identify where their position is based on interpretation rather than factual accuracy. Increased engagement between the FRC, FCA, Auditors and firms (as opposed to bilateral conversations) would be helpful in increasing consistency of approach of process, results, and the actual scope of what is being audited (for example, there is occasionally blurring of boundaries with some aspects of statutory audit, such as IT type control testing).

In order to address such issues and increase consistency, we support the concept of having a technical CASS advisory team within the FRC, which would have powers such as monitoring and inspection. The structure and scope of such powers would be critical to facilitate the right outcome and mitigating risk of audit becoming a “box ticking” process. With the right approach, such powers could support consistency in the interpretation of CASS requirements, opinion, and standard of work within both firms and auditors, as well as providing visibility as to how the standards underpin the effectiveness of governance over auditors. The FRC would of course need to be confident it has the resources to adequately undertake this role.

UK Finance strongly recommend the FRC formally consults with the industry in the development of such functions. A technical advisory team in the FRC, or with representatives across regulated firms, auditors, FRC and FCA would benefit all parties in reducing burden, cost and increasing usability and value in the audit reports.

(iii) Control function within firms

A common observation among our members is that an auditor’s own findings have reduced, and the auditors place an excessive reliance on the firm’s own identified breaches. For example, there are instances where auditors can be seen to be “reperforming” the activities already undertaken by a firm’s second and third Lines of Defense, and/or the control functions. The outcome is typically to reconfirm the firm’s own results, with no assessment provided on the quality and effectiveness of that work.

We would like to emphasise that it is to the credit of the firms themselves that there is a significant level of self-identifying breaches. Notwithstanding that the FCA is the final recipient of the report, it is neither helpful not valuable for a firm's Board to have a lengthy report outlining breaches that have already been identified using detective controls within the firm. We recommend where breaches have been self-identified by firms there should be a prominent method of highlighting this fact within the audit report.

The FRC standard encourages auditors to spend a significant proportion of time on controls testing. While we acknowledge that controls testing is important, the emphasis on this element could potentially be at the expense of increased substantive testing, for example end-to-end design, IT setup, and a more thorough assessment of Client Money reconciliation. UK Finance recommends that auditors should be able to place increased reliance on components of firms' own testing and increase emphasis on substantive testing, such as the examples provided, which would increase efficiency and the value proposition of the audit.

(iv) Proportionality

It would be beneficial for auditors to have discretion to apply materiality standards to audit finding. The effect would be to streamline the audit process and ensure that the resources of both firms and auditors are not be unduly expended in the case of de minimis breaches.

Auditors should also consider CASS risk when planning and executing their work, which would lead to a more targeted and proportionate approach when assessing the adequacy of a firm's protection of client assets. We recommend the FRC considers how proportionality can be increased in the auditing process.

(v) Risk-based approach

UK Finance does not believe a "one size fits all" auditing standard is the ideal approach across the spectrum of audited firms. We recommend the FRC considers implementing a "risk-based" approach instead, for example an in-depth SUP 3.10 audit every other year, with "lighter touch" audits in the intervening years, theme-based deep-dives on a periodic basis, and/or audit standards related to the size of the firm.

(vi) Results

The standards refer to the "beneficial client", rather than the "contracted client", as the end user, which could be interpreted as meaning the end user is the firms' client, rather than the firm itself, which should be clarified.

We recommend that the FRC gives consideration as to how the final audit results can provide more value to firms. For example, it would provide benefit to firms to have:

(i) Information identifying how the auditor has identified and addressed risk in their audit work.
(ii) An increase in the detail of information provided, for example, identification of themes, trend analysis, areas for improvement.
(iii) Greater focus on materiality.
(iv) An audit that reflects the idiosyncrasies of the firms rather than a standard, "one size fits all" approach.

We also recommend that as well as the points listed above, the FRC considers the issues raised throughout this response, as they are all themes and comments which can be fed into delivering greater benefit in the results of the audits, which is the ultimate objective of the whole process.

(vii) Cost

UK Finance acknowledges the critical nature of the CASS audit, and firms and auditors should be given sufficient lead time to implement any changes to the standards. However, it should be noted that for most firms the CASS audit is one of the most expensive regulatory audits. There are cases where firms are having to allocate further financial resources to external consultants to gain assurance of the technical elements of CASS which wouldn't be picked up as part of the annual CASS Audit under the new FRC Standards.
While we do not object to the process and the related cost, we ask the FRC to try to ensure that any future changes are as close to cost neutral as realistically possible, and give consideration as to how the value obtained can from the audits can be increased. UK Finance recommends using the comments provided in this response as a starting point for this analysis.