



# Scottish National Investment Bank plc

**Report to the Audit Committee**

Audit plan and strategy for the year ended 31 March 2023

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Report date : 9 November 2022

Meeting date: 16 November 2022

# Introduction

## About this report

This report has been prepared in accordance with the responsibilities set out within the Audit Scotland’s Code of Audit Practice (“the Code”).

This report is for the benefit of Scottish National Investment Bank Plc (“SNIB”) and is made available to Audit Scotland, the Auditor General and the Scottish Government, as a body (together “the Beneficiaries”). This report has not been designed to be of benefit to anyone except the Beneficiaries. In preparing this report we have not taken into account the interests, needs or circumstances of anyone apart from the Beneficiaries, even though we may have been aware that others might read this report. We have prepared this report for the benefit of the Beneficiaries alone.

Nothing in this report constitutes an opinion on a valuation or legal advice.

We have not verified the reliability or accuracy of any information obtained in the course of our work, other than in the limited circumstances set out in the scoping and purpose section of this report.

This report is not suitable to be relied on by any party wishing to acquire rights against KPMG LLP (other than the Beneficiaries) for any purpose or in any context. Any party other than the Beneficiaries that obtains access to this report or a copy (under the Freedom of Information Act 2000, the Freedom of Information (Scotland) Act 2002, through a Beneficiary’s Publication Scheme or otherwise) and chooses to rely on this report (or any part of it) does so at its own risk. To the fullest extent permitted by law, KPMG LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the Beneficiaries.

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# Introduction (continued)

## To the Audit Committee of Scottish National Investment Bank plc

I am pleased to have the opportunity to meet with you on 16 November 2022 to discuss our audit of the consolidated financial statements of Scottish National Investment Bank plc, as at and for the year ending 31 March 2023.

This report outlines our risk assessment and planned audit approach. I provide this report to you in advance of the meeting to allow you sufficient time to consider the key matters and formulate your questions.

## The engagement team

I am the engagement partner on the audit and am responsible for the audit opinion. I have over 23 years of experience with KPMG in the financial services industry and this will be my third year signing the audit opinion.

Other key members of the engagement team include Stephen Fisher (Senior Manager) with 15 years of financial services audit and industry experience.

## Scope definition

Audit Scotland has appointed KPMG LLP as auditor of SNIB in accordance with the Public Finance and Accountability (Scotland) Act 2000.

In addition to responsibilities under our appointment by Audit Scotland, SNIB has appointed us as auditor of its two subsidiaries – Scottish Investments Limited and Scottish Investments Services Limited.

We will also perform work in accordance with the wider responsibilities embodied in the Code of Audit Practice approved by the Commission and the Auditor General (see page 29).

## How we deliver audit quality

Audit quality is at the core of everything we do at KPMG and we believe that it is not just about reaching the right opinion, but how we reach that opinion. We consider risks to the quality of our audit in our engagement risk assessment and planning discussions.

We define ‘audit quality’ as being the outcome when audits are:

- **executed consistently**, in line with the requirements and intent of **applicable professional standards** within a strong **system of quality controls**; and
- all of our related activities are undertaken in an environment of the utmost level of **objectivity**, independence, **ethics** and **integrity**.

Yours sincerely



Philip Merchant

9 November 2022

# Overview of planned scope including materiality

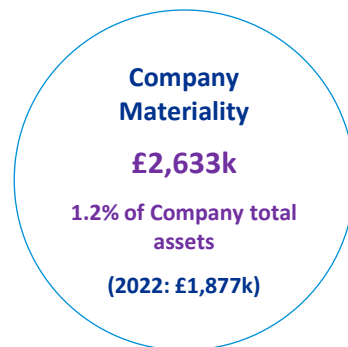
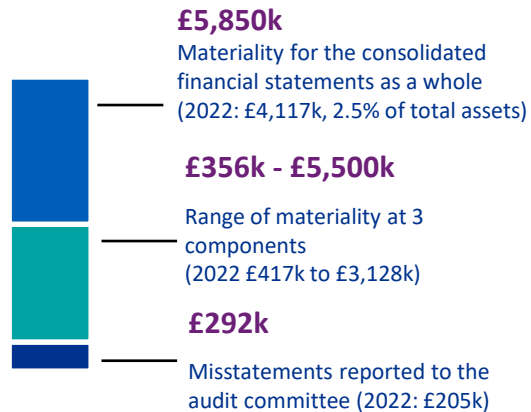
## Our materiality levels

We determined materiality for the consolidated financial statements at a level which could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements. We used a benchmark of total assets, which we consider to be appropriate given the sector in which the entity operates, its ownership and financing structure, and the focus of users.

We considered qualitative factors such as the maturity of SNIB's processes when determining materiality for the financial statements as a whole.

To respond to aggregation risk from individually immaterial misstatements, we design our procedures to detect misstatements at a lower level of materiality (£4,387k) driven by our evaluation of the potential for misstatements in the period. Our evaluation considers the history of misstatements, the control environment and other relevant factors. We also adjust this level further downwards for items that may be of specific interest to users for qualitative reasons, such as Directors' remuneration.

### Group materiality



## We will report misstatements to the audit committee including:

- Corrected and uncorrected audit misstatements above £292k for the Group and £131k for the Parent.
- Errors and omissions in disclosure (Corrected and uncorrected) and the effect that they, individually in aggregate, may have on our opinion.
- Other misstatements we include due to the nature of the item.

For Directors' remuneration (audited information within the Directors' Remuneration Report), we have assessed that a lower materiality is required to be applied as these figures are expected to be immaterial based on the overall materiality we have set for the Financial Statements as a whole, yet in our professional judgement these balances would be of interest to the shareholders of the Group. We have lowered the overall materiality for the Financial Statements as a whole to £1k (2022: £1k) for Directors' remuneration based on our professional judgement.

## Subsidiary materiality

Both subsidiaries are deemed significant components for group reporting and we will perform full scope audit to the materiality levels as disclosed below. The work will be performed by the same audit team.

	Materiality	Performance materiality	Audit misstatements
Scottish Investments Limited	£5,500k	£4,125k	£275k
Scottish Investment Services Limited	£356k	£267k	£18k

# Overview of planned scope including materiality (continued)

## Control environment

The impact of the group control environment on our audit is reflected in our planned audit procedures. Our planned audit procedures reflect findings raised in the previous year and management's response to those findings. We will continue to assess the impact of the current economic conditions on processes and controls, which may result in subsequent changes in our audit approach.

We will execute a substantive audit approach as the most effective and efficient method of addressing the identified risks of material misstatement. We will test the design and implementation of controls over journal entries.

## Timing of our audit and communications

We will maintain communication led by Phil and Stephen throughout the audit. We set out below the form, timing and general content of our planned communications:

- Audit Committee meeting on 16 November 2022 where we present our initial audit plan;
- Status meetings with management throughout the duration of our audit work;
- Audit committee meeting at the completion stage of the audit where we communicate the findings of our work, any audit misstatements and significant control deficiencies.

We plan to perform our audit work as follows:

- Planning and risk assessment will be completed prior to year end;
- As in the prior year, we expect to perform our audit work on unlisted investments to allow us to provide an interim update to the Audit Committee in May; and
- Other substantive procedures will be performed from April to June.

The year end timetable, including signing of financial statements has been discussed but is yet to be agreed with management.

## Our fees

We have included details of our fee proposal on page 17 and will be happy to discuss the fees at the meeting.

## Wider scope

The Code of Audit Practice has refreshed the areas used to define the wider audit scope. The previous 2016 edition set out four areas (described as audit dimensions), i.e. financial management, financial sustainability, governance and transparency, and value for money. The new Code no longer uses the term audit dimensions, but it retains the areas of financial management and financial sustainability (though redefines each area) and replaces the other two as follows:

- governance and transparency dimension has been replaced with vision, leadership and governance area
- value for money dimension has been replaced with use of resources to improve outcomes.

Our audit will take the above areas into account in its execution.

## Revenue recognition – rebuttal of fraud risk

Professional standards require us to presume, unless rebutted, that the fraud risk from revenue recognition is a significant risk. We have assessed that the fraud risk is not significant due to the relative simplicity of revenue transactions and sources.

## Impacts of climate risk and new ESG/climate change disclosures

We will evaluate management's assessment of the potential financial implications of climate risk on the financial statements, including estimates and disclosures.

As part of our procedures on other information, we will obtain and read your ESG/climate change disclosures. We will consider whether there is a material inconsistency between this information include in the annual report and the financial statements, or with our knowledge obtained in the audit; or whether this information appears to be materially misstated.

# Group audit scope

Both subsidiaries are deemed significant components for group reporting and we will perform full scope audit to the component materiality. The work will be performed by the same audit team.

The application of the significant risks and other areas of focus to each group entity is summarised in the table below.

	Scottish National Investment Bank plc (Parent)	Scottish Investments Limited (SIL)	Scottish Investments Services Limited (SISL)
<b>Significant Risks</b>			
1. Management override of controls	Y	Y	Y
2. Valuation of unlisted investments		Y	
<b>Other Areas of Audit Focus</b>			
3. Recoverability of parent's debt due from group entities	Y		
4. Going concern	Y	Y	Y
5. Expenses			Y
6. Cash	Y	Y	Y

# Significant risks and other areas of audit focus

Our risk assessment draws upon our historic knowledge of the business, the industry and the wider economic environment in which SNIB operates.

We also use our regular meetings with senior management to update our understanding.

The risk map shows the identified significant risks and other areas of audit focus, subject to the completion of our risk assessment procedures.

Our long form audit report will include details of our findings in relation to significant financial statement audit risks and key audit matters.

## Significant risks

Management override of control is a significant risk that professional standards require us to assess in all cases.

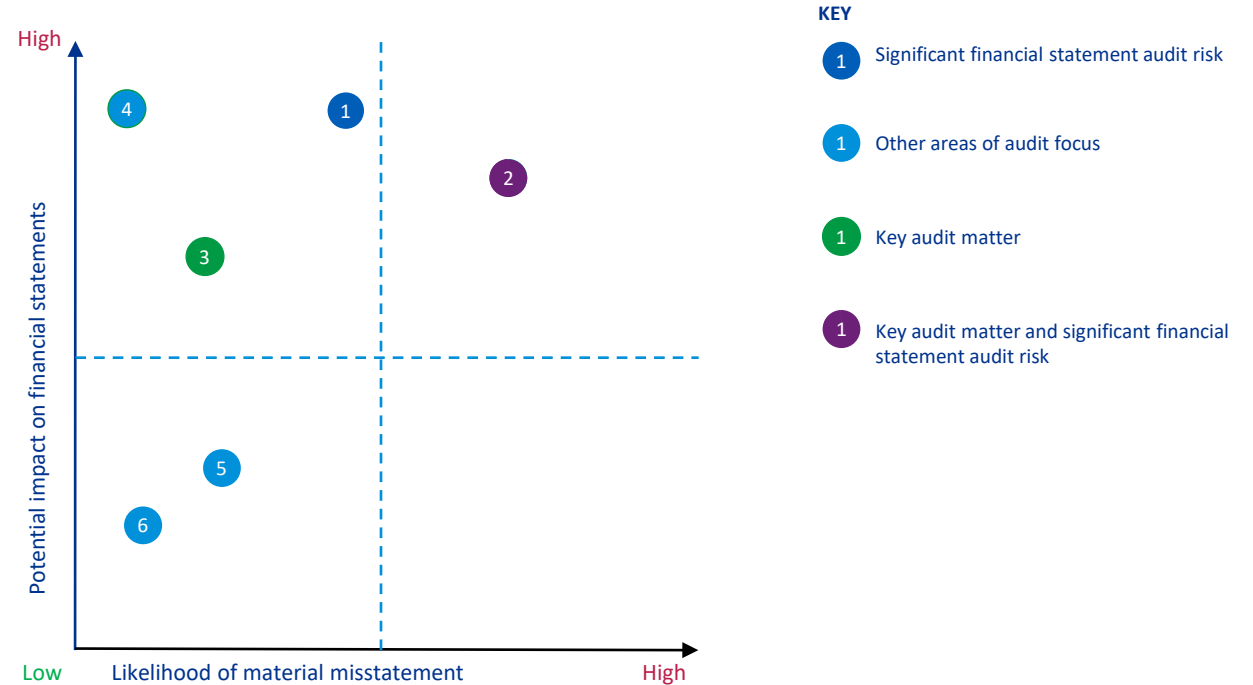
Valuation of unlisted investments is considered to be a significant risk due to a significant estimation uncertainty around the valuations and further complexity in relation to macroeconomic factors.

We also recognise a key audit matter for the parent financial statements in relation to the recoverability of debt due from group entities.

## 2023 Risk Assessment updates

Based upon our experience of auditing the 2022 financial statements we have removed financial reporting as an area of further focus as we recognise the increased resources involved in the process and reduced audit misstatements identified.

Given the impact of COVID on financial markets has now reduced we have not included this within the going concern risk. We do continue to see volatility in the performance of financial markets led by a number of global factors and our risk assessment will be a continuum as we go through the FY23 cycle.



### Significant Risks

- ① Management override of controls
- ② Valuation of unlisted investments (Key audit matter)

### Other Areas of Audit Focus

- ③ Recoverability of parent's debt due from group entities (key audit matter for the parent)
- ④ Going concern
- ⑤ Expenses
- ⑥ Cash

# Significant risks

1

## Management Override of Controls <sup>(a)</sup>

Fraud risk related to unpredictable way management override of controls may occur

### Significant audit risk

#### The risk

- Professional standards require us to communicate the fraud risk from management override of controls as significant.
- Management is in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.
- We have not identified any specific additional risks of management override relating to this audit.

### Planned response

- Our audit methodology incorporates the risk of management override as a default significant risk.
- In line with our methodology, we will test the design and implementation of controls over journal entries and post-closing adjustments.
- We will set high risk criteria for specific journals to test substantively. If any journals meet this criteria, we will audit each journal individually as part of our year end audit process.
- We will assess the appropriateness of changes to the methods and underlying assumptions used to prepare accounting estimates.
- We will assess the appropriateness of the accounting for significant transactions that are outside the Group's normal course of business, or are otherwise unusual as applicable.

Note: (a) Significant risk that professional standards require us to assess in all cases.



# Significant risks (continued)

2

## Valuation of unlisted investments

Risk that the carrying value of unlisted investments is materially misstated

### Significant audit risk and key audit matter

#### The risk

- The Group's portfolio of unlisted investments makes up 85% (2022: 92%) of the total assets (based on the draft trial balance as at 30 September 2022). Unlisted investments are measured at fair value, which is established in accordance with the International Private Equity and Venture Capital Valuation Guidelines by using measurements of value such as prices of recent orderly transactions, earnings multiples and net assets.
- The effect of these matters is that, as part of our risk assessment, we determined that the valuation of unlisted investments has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole.

### Planned response

- **Methodology choice:** In the context of observed industry best practice and the provisions of the International Private Equity and Venture Capital Valuation Guidelines, we will challenge the appropriateness of the valuation basis selected.
- **Our valuations experience:** We will challenge the directors on key judgements affecting investee company valuations, such as the choice of benchmark for earnings multiples. We will compare key underlying financial data inputs to external sources, investee company audited accounts and management information as applicable. We will challenge the assumptions around sustainability of earnings based on the plans of the investee companies and whether these are achievable. Our work will include consideration of events which occur subsequent to the year end up until the date our audit report.
- **Comparing valuations:** Where a recent transaction is used to value a holding, we will obtain an understanding of the circumstances surrounding the transaction and whether it is considered to be on an arm's length basis and suitable as an input into a valuation.
- **Assessing transparency:** We will consider the appropriateness, in accordance with relevant accounting standards, of the disclosures in respect of unlisted investments and the effect of changing one or more inputs to reasonably possible alternative valuation assumptions.

We will perform risk assessment procedures to determine the level of work required over each asset in the portfolio. This will incorporate the risk assessment prepared by management and the nature and size of each investment.

# Other areas of audit focus

3

Recoverability of parent's debt due from group entities (key audit matter – parent)

Risk related to recoverability of intra-group loan from the parent to subsidiary

## Key audit matter (parent)

### The risk

- The carrying amount of the intra-group debtor balance represents 95% (2022: 99%) of the Company's total assets. The recoverability is not at a high risk of significant misstatement or subject to significant judgement. However, due to its materiality in the context of the financial statement, this is considered to be an area that will have the greatest effect on our overall parent company audit. Note: This risk is applicable to the parent only.

## Planned response

- **Test of detail:** We will assess whether the debtor company has a positive net asset value and therefore coverage of the debt owed, as well as assessing whether the debtor company has historically been profit-making.
- **Assessing the subsidiary company audit:** We will assess the work performed on the subsidiary company audit, and considering the results of that work, on those net assets, including assessing the liquidity of the assets and therefore the ability of the subsidiary to fund the repayment of the receivable.

# Other areas of audit focus (continued)

4

## Going concern

Ability of the business to continue as a going concern

### Other areas of audit focus

#### The risk

- Management's assessment of the Group's ability to continue as a going concern involves consideration of all factors affecting the Group.
- There is a risk that management's assessment of the Group's ability to continue as a going concern does not appropriately consider the impact of all external factors, including plausible but severe downside scenarios on the income and carrying value of assets.
- The risk that disclosures in the financial statement and the annual report are not adequate with regard to the effect of key risks to the financial position, performance, business model and strategy.

### Planned response

- Evaluate how management's risk assessment process identifies business risks relating to events and conditions that may cast significant doubt on the ability to continue as a going concern.
- Evaluate any models management uses in its assessment and evaluate how the information system captures events and conditions that may cast significant doubt on ability to continue as a going concern.
- Evaluate whether management's assessment has failed to identify events or conditions that may cast significant doubt on going concern and whether the method used by management is appropriate.
- Assess management's going concern assessment including the plausible but severe downside scenarios particularly whether those downside scenarios reflect plausible external impacts on the business.
- Evaluate whether sufficient and appropriate audit evidence has been obtained to conclude whether a material uncertainty exists and the appropriateness of management's use (or otherwise) of the going concern basis of accounting.
- Evaluate whether there is adequate support for the assumptions underlying management's assessment, whether they are realistic and achievable and consistent with the external and/or internal environment and other matters identified in the audit.
- Challenge management's plans for future actions, and verify the reliability and relevance of data used. Determine whether the outcome of these plans is likely to improve the situation and whether management's plans are feasible.
- We will inspect letters received by the directors indicating Scottish Government's intention to provide this support and will assess the business reasons why Scottish Government may or may not choose to provide this support.

# Other areas of audit focus (continued)

5

Expenses

Expenses may be materially misstated

## Other areas of audit focus

### The risk

- Expenses could be recorded in the incorrect year (cut-off), at the incorrect amount (accuracy) or not recorded at all (completeness).

## Planned response

- We will trace a sample of administrative expenses and staff costs transactions back to the supporting documentation and to bank statements.
- We will review a sample of payments made post year end to identify expenses that may have been omitted in the year.

# Other areas of audit focus (continued)

6

Cash

Cash balances may be materially misstated

## Other areas of audit focus

### The risk

- Cash balances, as reported by management, may not be complete or accurate, or the company may not have the rights to ownership of the bank accounts.

## Planned response

- All year end cash balances recorded in the financial statements will be agreed to third party confirmations received independently. We will investigate any reconciling items above our reporting threshold.
- We will test the design and implementation and operating effectiveness of controls over bank reconciliations.

# Mandatory communications

Type	Statements
<b>Management’s responsibilities (and, where appropriate, those charged with governance)</b>	<p>Prepare financial statements in accordance with the applicable financial reporting framework that are free from material misstatement, whether due to fraud or error.</p> <p>Provide the auditor with access to all information relevant to the preparation of the financial statements, additional information requested and unrestricted access to persons within the entity.</p>
<b>Auditor’s responsibilities</b>	<p>The Audit Scotland letter of appointment and Code of Practice and our subsidiary engagement letters communicate our responsibilities to form and express an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities.</p>
<b>Auditor’s responsibilities – Fraud</b>	<p>This report communicates how we plan to identify, assess and obtain sufficient appropriate evidence regarding the risks of material misstatement of the financial statements due to fraud and to implement appropriate responses to fraud or suspected fraud identified during the audit.</p>
<b>Auditor’s responsibilities – Other information</b>	<p>The Audit Scotland letter of appointment and Code of Practice and our subsidiary engagement letters communicate our responsibilities with respect to other information in documents containing audited financial statements. We will report to you on material inconsistencies and misstatements in other information.</p>
<b>Independence</b>	<p>Our independence confirmation letter on page 16 discloses matters relating to our independence and objectivity including any relationships that may bear on the firm’s independence and the integrity and objectivity of the audit engagement partner and audit staff.</p>

# Appendix

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# Confirmation of independence

**We confirm that, in our professional judgement, KPMG LLP is independent within the meaning of regulatory and professional requirements and that the objectivity of the engagement partner and audit staff is not impaired.**

To the Audit Committee

## **Assessment of our objectivity and independence as auditor of Scottish National Investment Bank Plc and its subsidiaries (“the Group”)**

Professional ethical standards require us to provide to you at the planning stage of the audit a written disclosure of relationships (including the provision of non-audit services) that bear on KPMG LLP’s objectivity and independence, the threats to KPMG LLP’s independence that these create, any safeguards that have been put in place and why they address such threats, together with any other information necessary to enable KPMG LLP’s objectivity and independence to be assessed.

This letter is intended to comply with this requirement and facilitate a subsequent discussion with you on audit independence and addresses:

- general procedures to safeguard independence and objectivity;
- independence and objectivity considerations relating to the provision of non-audit services; and
- independence and objectivity considerations relating to other matters.

### **General procedures to safeguard independence and objectivity**

KPMG LLP is committed to being and being seen to be independent. As part of our ethics and independence policies, all KPMG LLP partners and staff annually confirm their compliance with our ethics and independence policies and procedures including in particular that they have no prohibited shareholdings. Our ethics and independence policies and procedures are fully consistent with the requirements of the FRC Ethical Standard. As a result we have underlying safeguards in place to maintain independence through:

- instilling professional values;
- communications;
- internal accountability;
- risk management;
- independent reviews.

We are satisfied that our general procedures support our independence and objectivity.

### **Independence and objectivity considerations relating to the provision of non-audit services**

We have not provided any non-audit services to the Group.

### **Application of the FRC Ethical Standard 2019**

That standard became effective for the first year commencing on or after 15 March 2020, except for the restrictions on non-audit and additional services that became effective immediately at that date, subject to grandfathering provisions.

We confirm that as at the date of this document we are not providing any non-audit or additional services that required to be grandfathered.

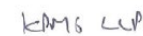
### **Confirmation of audit independence**

We confirm that as of the date of this letter, in our professional judgement, KPMG LLP is independent within the meaning of regulatory and professional requirements and the objectivity of the Partner and audit staff is not impaired.

This report is intended solely for the information of the Audit Committee of the Group and should not be used for any other purposes.

We would be very happy to discuss the matters identified above (or any other matters relating to our objectivity and independence) should you wish to do so.

Yours faithfully



KPMG LLP





# Audit fees

## Fee proposal for year ended 31 March 2023

We recognise the need for competitive fees and we wish to provide value. We believe in being very open in the way we deal with audited entities and our approach to fees is no different.

Audit quality is our number one priority, and we are committed to delivering consistently high-quality audits. We've made good progress supported by our record levels of investment but there is still more to do. We are committed to continuous improvement and investment.

We have estimated the audit fee based on our understanding of the portfolio at 31 October 2022. As noted below, the fee will be revised based on our risk assessment procedures, review of valuation methodology for debt and convertible loan note investments and changes to the portfolio prior to year end.

Entity	2022	Inflation	ISA changes	Investment portfolio	Total
SNIB	70,000	7,000	3,500	-	80,500
SIL	52,250	5,225	1,163	28,600-51,400	87,238-110,038
SISL	24,645	2,465	1,232	-	28,342
<b>Total</b>	<b>146,895</b>	<b>14,690</b>	<b>5,895</b>		<b>196,079-218,879</b>

## Scope changes from prior year

The following changes in scope are applicable to the year ended 31 March 2023:

- Inflation – we are facing significant inflationary pressures in relation to staff costs and recruitment. Professional services firms are seeing wage inflation significantly in excess of wider RPI or CPI inflation, and audit firms globally are engaged in a 'war for talent'. Recent announcements by ourselves, and other audit firms, regarding out of cycle pay increases are required to enable us to recruit and retain good people, and provide continuity on our engagement teams.
- ISA changes – As detailed on pages 19 to 21, ISA 315 and ISA 240 have been revised to require a more robust risk identification and assessment by audit teams; thereby promoting more specificity in response to the identified risks. It includes both new and enhanced requirements. We expect an incremental impact of 5% to 20% on base audit costs. The scope change included above is at the lower end of that range.

- Investment portfolio – the audit fee for SIL is dependent on the size and complexity of the investment portfolio at year end. The estimate above has been calculated based on the 25 investments in the portfolio at 31 October 2022 and will be revised once we receive the year end portfolio. We also highlight that we have not yet completed our risk assessment procedures over investment valuations and will revise our fee proposal accordingly. The fee charged per investment reflects the work required to audit unlisted investments and has been benchmarked to fee levels for similar audited entities.

## Revision of fee estimate

As in the prior year, we will revise our fee estimate as we approach year end, taking into account:

- The size and composition of the portfolio at year end;
- The results of risk assessment procedures over the portfolio as discussed on page 9; and
- Discussion with management about how to make the audit as efficient as possible.

We will provide an update at future audit committee meetings.

## CASS audit

- The fees above do not include any CASS audit that may be required for SIL depending on the timing of permissions approval by FCA.
- We are currently discussing the expected permissions, timing of authorisation and the impact on audit requirements.
- If we are engaged to deliver this work, the fee for it will be agreed separately.

# ISA (UK) 315 Revised: Overview



## Summary

ISA (UK) 315 *Identifying and assessing the risks of material misstatement* incorporates significant changes from the previous version of the ISA. These have been introduced to achieve a more rigorous risk identification and assessment process and thereby promote more specificity in the response to the identified risks. The revised ISA is effective for periods commencing on or after 15 December 2021.

The revised standard expands on concepts in the existing standards but also introduces new risk assessment process requirements – the changes will have a significant impact on our audit methodology and therefore audit approach.

### Why have these revisions been made?

With the changes in the environment, including financial reporting frameworks becoming more complex, technology being used to a greater extent and entities (and their governance structures) becoming more complicated, standard setters recognised that audits need to have a more robust and comprehensive risk identification and assessment mechanism.

The changes are aimed at (i) promoting consistency in effective risk identification and assessment, (ii) modernising the standard by increasing the focus on IT, (iii) enhancing the standard’s scalability through a principle based approach, and (iv) focusing auditor attention on exercising professional scepticism throughout risk assessment procedures.

### What does this mean for an audit?

To meet the requirements of the new standard, auditors will be required to spend an increased amount of time across the risk assessment process, including more detailed consideration of the IT environment. We expect these changes to result in significantly increased audit effort levels which will, in turn, affect auditor remuneration. This additional effort is a combination of time necessary to perform the enhanced risk assessment procedures and the anticipated need to involve more technical specialists (particularly IT Audit professionals) in our audits.

Given the level of changes to the standard, debate remains ongoing about the extent of impact on application of some paragraphs. Global regulators have committed to providing further clarification in this area in advance of adoption, and there may therefore be some later updates to our initial assessment of relative impact.

Expected effect on audit effort	
Increased professional scepticism	
Understanding the entity	
Understanding internal control	
IT systems and communication	
Control activities	
Identifying and assessing risks	
Control risk	
Stand-back assessment and documentation	
Total effort	

# ISA (UK) 315 Revised: Summary of key changes



Area	Impact on audit effort	Summary of changes and impact
Increased professional scepticism		<p>Increased focus on applying professional scepticism – particularly the need for auditors not to bias their approach towards obtaining evidence that is corroborative in nature or excluding contradictory evidence, which requires more independent evidence to be sought. In all cases, there will be enhanced documentation requirements in this area.</p>
Understanding the entity		<p>Requirements to obtain an understanding of the entity have been restructured and enhanced. The changes are focused on the importance of understanding the applicable financial reporting framework and the entity's accounting policy choices, as well as the extent of IT usage in the business' processes. This will result in increased risk assessment procedures and documentation requirements.</p>
Understanding internal control		<p>The previous standard included requirements for understanding components of the entity's system of internal control. The revisions add another step by requiring auditors perform evaluation procedures over these. This may require additional effort to evaluate the entity's processes over risk assessment and monitoring activities over internal control systems to assess their appropriateness to the entity's size and complexity.</p>
IT systems and communication		<p>The requirements introduce an increased focus on understanding the entity's own management of IT. This may entail performing additional risk assessment procedures and taking a broader view across the IT environment, considering more systems and systems in greater depth, than previously. Given the complexity and specialist knowledge required to perform these procedures, increased use of IT Auditors will be a natural consequence of this revision.</p>
Control activities		<p>The revised standard enhances the way we identify IT applications and aspects of the IT environment that are subject to assessed risks arising from IT. This may result in significant expansion of risk assessment procedures to obtain and evaluate the necessary information. Further, the standard adds new requirements in control testing activities to mandate evaluation of general IT controls that address risks arising from IT associated with significant risks and certain journal entries. For these controls, the auditor is required to evaluate the design and implementation of the individual controls. This could result in a significant change in approach, with more emphasis and effort spent on evaluating control activities. Again, we anticipate integrating more specialised expertise into our audit team to meet the revised requirements.</p>
Identifying and assessing risks		<p>The changes require more detailed assessment of risks at both the financial statement and assertion levels for classes of transactions, account balances and disclosures than previously. Further, the revisions introduce an inherent risk spectrum and new inherent risk assessment factors, each of which the auditor evaluates to assess the level of risk and thereby shape the audit response. This will increase the audit effort needed to evaluate and document the risks of material misstatement.</p>
Control risk		<p>New requirement to assess inherent risk and control risk separately for each risk of material misstatement identified where the auditor plans to test the operating effectiveness of controls. The separation of assessments will require individual attention, increased documentation and is likely to affect sample sizes for substantive procedures.</p>
Stand-back assessment		<p>New requirement to perform a stand-back assessment for material classes of transactions, account balances or disclosures which have not been identified as significant, to assess whether this determination remains appropriate in the context of the overall audit. This will require increased consideration of aggregation risk and introduce additional documentation requirements.</p>

# ISA (UK) 240 Revised: Summary of key changes



Summary and background	Area	Summary of changes and impact	Effect on audit effort
<p>ISA (UK) 240 <i>The auditor's responsibilities relating to fraud in an audit of financial statements</i> includes revisions introduced to clarify the auditor's obligations with respect to fraud and enhance the quality of audit work performed in this area. The revised ISA (UK) is effective for periods commencing on or after 15 December 2021. Unlike ISA (UK) 315 which mirrors updates in the international ISA, the updated UK fraud standard is not based on international changes by the IAASB.</p> <p>The impact of the revisions to ISA (UK) 240 is less extensive compared to ISA (UK) 315, but will nevertheless result in changes to our audit approach. The table below summarises the main changes and our initial assessment of their impact.</p>	<p>Risk assessment procedures and related activities</p>	<p>[1] Increased focus on applying professional scepticism – the key areas affected are:</p> <ul style="list-style-type: none"> <li>— the need for auditors not to bias their approach towards obtaining evidence that is corroborative in nature or excluding contradictory evidence,</li> <li>— remaining alert for indications of inauthenticity in documents and records, and</li> <li>— investigating inconsistent or implausible responses to inquiries performed.</li> </ul> <p>[2] Requirements to perform inquiries with individuals at the entity are expanded to include, amongst others, those who deal with allegations of fraud.</p> <p>[3] Every audit now requires a specific determination as to whether to involve technical specialists (including forensics) to aid in identifying and responding to risks of material misstatement due to fraud. This will result in increased involvement of specialists and an expanded scope of work for these specialists, on audit engagements.</p>	
	<p>Internal discussions and challenge</p>	<p>Enhanced requirements for internal discussions among the audit team to identify and assess the risk of fraud in the audit, including a requirement to determine the need for additional meetings to consider the findings from earlier stages of the audit and their impact on our assessment of the risk of fraud.</p>	
	<p>Communications with management / TCWG</p>	<p>New requirements for communicating matters related to fraud with management and those charged with governance, in addition to the reporting in our audit reports.</p>	

## What does this mean for an audit?

The changes introduce new requirements which will increase audit effort and therefore the audit fee. The additional work is largely the result of investing more time identifying and assessing the risk of fraud during risk assessment and involving specialists to aid with both risk identification and the auditor's response to risk.

# Subsidiary audit exemption

The Companies Act allows UK groups that produce consolidated accounts to take advantage of the audit exemption for any UK subsidiaries included within the consolidated accounts provided that the parent company is willing to provide a parent company guarantee.

01

## Which companies can use the subsidiary audit exemption?

UK subsidiaries which are included within UK consolidated accounts can elect to take the audit exemption, provided they do not have listed shares or debt and certain other restrictions. Please see the link below for the full listing of companies unable to take the exemption.

02

## What is the impact of taking the audit exemption?

The parent company is guaranteeing the liabilities of the subsidiary that exist as at the balance sheet date for the life of the liability and careful consideration of the risks that this entails needs to be undertaken before giving the guarantee as this increases the risk to the parent company. Intermediate holding companies with no external liabilities or contingent liabilities may be the most suitable to take the exemption.

03

## How do we claim the exemption?

The consolidated accounts need to state that subsidiary X is in receipt of a parental guarantee to take advantage of the audit exemption for that year. The [ICAEW Technical Release](#) provides details of the forms to submit to Companies House to take the exemption. This process must be repeated for all subsequent years where the company wishes to make use of the exemption.

04

## Audit implications

The parent company's going concern evaluation, which its auditors would then need to evaluate, would need to examine the likelihood and impact of the guarantee being called upon to settle the liabilities of the subsidiary receiving the guarantee.

05

## Where can I find further guidance?

Further guidance setting out which entities are eligible and the process that needs to be taken to apply the audit exemption can be found at <https://www.icaew.com/technical/technical-releases/legal/tech-0620bl-exemption-from-audit-by-parent-guarantee>.

# Newly effective standards

Standards	Expected impact				Effective for years beginning on or after	
	High	Moderate	Low	None	1 January 2022	1 January 2023
<a href="#"><i>Onerous Contracts – Cost of Fulfilling a Contract (Amendments to IAS 37)</i></a>				○	✓	
<a href="#"><i>Annual Improvements to IFRS Standards 2018-2020</i></a>			●		✓	
<a href="#"><i>Property, Plant and Equipment: Proceeds Before Intended Use (Amendments to IAS 16)</i></a>			●		✓	
<a href="#"><i>Reference to the Conceptual Framework (Amendments to IFRS 3)</i></a>				○	✓	
<a href="#"><i>Classification of Liabilities as Current or Non-current (Amendments to IAS 1)</i></a>			●			✓
<a href="#"><i>IFRS 17 Insurance contracts</i></a>				○		✓
<a href="#"><i>Accounting Policies, Changes in Accounting Estimates and Errors: definition (Amendments to IAS 8)</i></a>			●			✓
<a href="#"><i>Amendments to IAS 1 Presentation of Financial Statements and IFRS Practice Statement 2 Making Materiality Judgements</i></a>			●	○		✓
<a href="#"><i>Deferred Tax Related to Assets and Liabilities Arising from a Single Transaction – Amendments to IAS 12 Income Taxes</i></a>			●	○		✓

# FRC's areas of focus

The areas of focus from the [FRC's Annual Review of Corporate Reporting 2020/21](#), annual letter to CEOs, CFOs and audit committee chairs along with the five thematic reviews issued in 2021 should be considered for reporting in the current financial period. The reports identify where the FRC believes companies should be improving their reporting. Below is a high level summary of the key topics. We encourage management and those charged with governance to read further on those areas which are significant to the group.

## Judgements and Estimates



In the current climate it is particularly important for Companies to provide as much context as possible for the assumptions and predictions underlying the amounts recognised in the financial statements, including potential sensitivities or ranges of possible outcomes.

Companies should disclose the carrying amounts impacted by estimation uncertainty. Disclosures of key assumptions and sensitivities could be improved. Preparers are encouraged to clearly distinguish between sources of estimation uncertainty with a significant risk of a material adjustment in the following year and other, perhaps longer-term, uncertainties.

Significant accounting judgements should be clearly explained along with factors considered.

## Revenue



Having raised a considerable number of queries in relation to revenue recognition policies and related disclosure, the FRC strongly encourage preparers to read their thematic report which includes tips and examples of good and inadequate disclosure.

Companies should disclose significant judgements made in accounting for revenue. This could include judgements in relation to performance obligations, transaction price and amounts allocated to performance obligations. Disclosures should clearly identify the methods used to estimate any variable consideration, including the application of the constraint. The FRC notes that disclosure of a significant risk of a downward adjustment to revenue suggests that the variable constraint may not have been applied appropriately.

## Statement of Cash Flows



Companies need robust reviews of the cash flow statement to ensure consistency with other parts of the annual report and to ensure preparation in line with the accounting standard.

Errors continue to be identified, including inappropriate classification of cash flows and inappropriate netting. The FRC also challenges companies on the composition of cash equivalents and on incomplete or incorrect related disclosures.

Companies are reminded that even in the limited cases where borrowings can be included as a component of cash and cash equivalents in the cash flow statement, the IAS 32 'Financial Instruments: Presentation' criteria need to be applied to determine whether they can be presented on a net basis in the balance sheet.

## Alternative Performance Measures (APMs)



APMs should not be given undue-prominence. Preparers should avoid statements appearing to provide APMs with more authority than IFRS measures and are reminded that meaningful commentary on the IFRS figures is required.

APMs, including ratios, should be appropriately labelled and reconciled to the most directly reconcilable financial statement line item. It should be clear how reconciling items are determined and companies should explain clearly why amounts are excluded from adjusted measures. Adjusting items should include gains as well as losses, where relevant.

# FRC's areas of focus (continued)

## Impairment of Assets



- [FRC Thematic Review](#)
- [2020 Review of Climate Related Considerations](#)

Impairment remains an area of focus in light of continued COVID-19 uncertainty and the risks related to climate change. Companies need to consider the impact of climate change on impairment reviews, especially in industries where investors may reasonably expect climate changes to significantly affect future expected cash flows.

When uncertainties indicate possible impairment, disclosures should indicate whether impairment tests have been performed and explain and quantify the key assumptions (including when parent company investments in subsidiaries are assessed, for example when the net assets of the parent company exceed market capitalisation).

Preparers are also encouraged to provide clear disclosures the effect of reasonably possible changes to clear assumptions.

## Financial Instruments



- [FRC's Thematic Review](#)
- [Case Study](#)

Factoring and reverse factoring arrangements require transparent disclosures, covering the nature of any material arrangements, the liquidity implications and the relevant amounts.

If significant judgement is required to determine the appropriate accounting or measurement basis, then it is expected that the basis of this judgement will be explained in the disclosure.

Non-banking preparers should ensure that they properly apply the credit risk-related disclosures such as the inputs, assumptions and estimation techniques used to measure impairment, amounts by credit risk rating grades, information about credit risk management practices and the concentration of credit risk, where material.

The FRC expect companies to provide information about their banking covenants unless the likelihood of any breach is considered remote.

## Strategic Report



The strategic report should provide a fair, balanced and comprehensive analysis of the development and performance of the business in the financial year and of its position at the end of the year. In particular companies are encouraged to include discussion of relevant significant matters and performance against key strategic objectives e.g. discussion of cash flow performance where cash generation is a key strategic action.

## Provisions and contingencies



Provisions and contingencies should be clearly explained including the nature of the exposure, the timeframe and the basis for determining the amount. Any significant judgements and relevant assumptions should be disclosed clearly.

There should be consistency between information provided in the annual report and accounts.

If material provisions are dependent on the future performance of a business expected to be heavily impacted by climate change, this should be disclosed and detail provided on how climate change had been taken into account in the estimate.

## Leases



Lessees and lessors are required to disclose information that gives a basis for users to assess the effect of leases on financial position, financial performance and cash flows. This could include information about variable payment features, for example. Judgements should be disclosed.

Entity-specific accounting policies should be disclosed for material transactions.



# FRC's areas of focus (continued)

## Income Taxes



Where a loss-making entity is recognising deferred tax assets (DTAs) and utilisation depends on future profits, entities are required to disclose the amount of the DTA, the nature of the evidence considered, any critical judgements used in the recognition of the DTAs and the key sources of estimation uncertainty.

## 2021/22 priorities for FRC review:



- **Impact of COVID-19**
- **Climate Change (FRC Thematic Review 2020 and 2021)**

In addition to the 'top ten' topics summarised above, the FRC have indicated that routine monitoring for the 2021/22 cycle will include a focus on:

- judgement and uncertainty in the face of continuing economic and social impact of Covid-19; and
- climate-related risks and new disclosures.

Disclosure on judgements and assumptions about the future will remain important to users of reports, particularly when considering matters such as going concern and liquidity. Therefore as part of their routine 2021/22 routines, the FRC will continue to consider whether companies:

- explain the significant judgements and estimates made;
- provide meaningful sensitivity analysis or details of a range of possible outcomes;
- describe any significant judgements made in determining whether there is a material uncertainty about their ability to continue as a going concern; and
- ensure that assumptions used in the going concern assessment are compatible with those used elsewhere.

For accounting periods beginning on or after 1 January 2021, premium listed companies will be required to disclose their compliance with the Taskforce for Climate-related Financial Disclosures (TCFD) recommendations on a comply-or-explain basis. To achieve this they must include a statement in their annual financial report setting out:

- whether they have made disclosures consistent with the recommendations of the TCFD;
- where the disclosures are instead in a document outside of the annual financial report, an explanation of why and a reference to where they can be found; and
- where disclosures are not made, an explanation of why, and a description of any steps taken or planned to be able to make consistent disclosures in the future, including time frames.

Furthermore, proposals for mandatory climate-related financial disclosure requirements for PLCs, large private companies and Limited Liability Partnerships have been consulted on. It is proposed that regulations will come into force for periods starting on or after 6 April 2022, for entities meeting the following requirements:

- all UK companies that are currently required to produce a non-financial information statement;
- UK registered companies admitted to AIM with more than 500 employees; and
- other meeting companies meeting the definition of 'large'

# KPMG's audit quality framework

Audit quality is at the core of everything we do at KPMG and we believe that it is not just about reaching the right opinion, but how we reach that opinion.

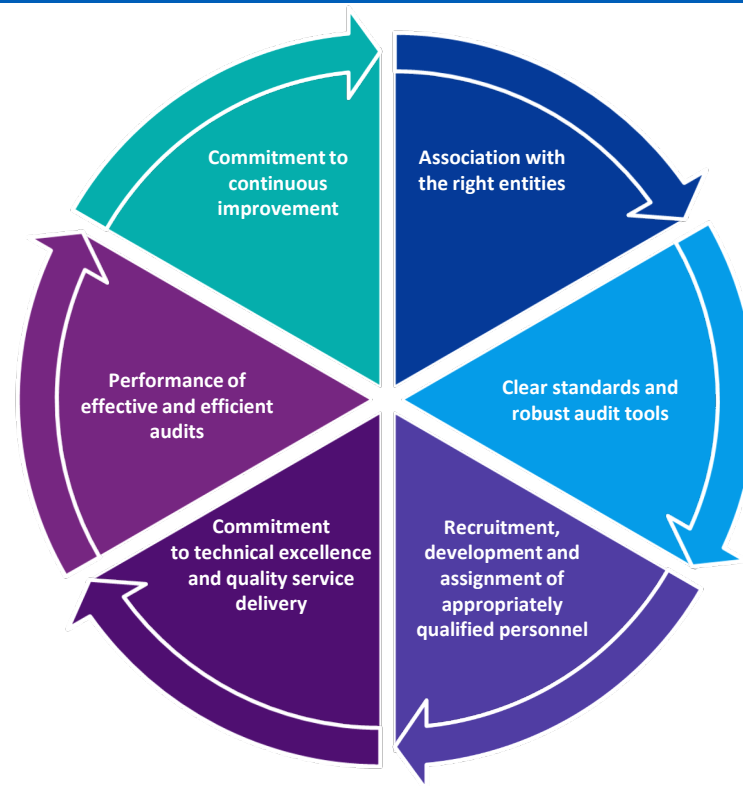
To ensure that every partner and employee concentrates on the fundamental skills and behaviours required to deliver an appropriate and independent opinion, we have developed our global Audit Quality Framework.

Responsibility for quality starts at the top through our governance structures as the UK Board is supported by the Audit Oversight Committee, and accountability is reinforced through the complete chain of command in all our teams.

- Comprehensive effective monitoring processes
- Significant investment in technology to achieve consistency and enhance audits
- Obtain feedback from key stakeholders
- Evaluate and appropriately respond to feedback and findings

- Professional judgement and scepticism
- Direction, supervision and review
- Ongoing mentoring and on the job coaching, including the second line of defence model
- Critical assessment of audit evidence
- Appropriately supported and documented conclusions
- Insightful, open and honest two way communications

- Technical training and support
- Accreditation and licensing
- Access to specialist networks
- Consultation processes
- Business understanding and industry knowledge
- Capacity to deliver valued insights



- Select entities within risk tolerance
- Manage audit responses to risk
- Robust client and engagement acceptance and continuance processes
- Client portfolio management

- KPMG Audit and Risk Management Manuals
- Audit technology tools, templates and guidance
- KPMG Clara incorporating monitoring capabilities at engagement level
- Independence policies

- Recruitment, promotion, retention
- Development of core competencies, skills and personal qualities
- Recognition and reward for quality work
- Capacity and resource management
- Assignment of team members, specialists and specific team members

# Investing in audit quality

01

## Engaging with our stakeholders

 2,800

Members of our UK Audit Committee Institute

£10tn > FTSE350 market cap

Value of assets under management of institutional investors attending our events

92

Number of individual contact points with institutional investors and investor associations

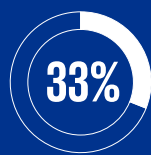


79%

FTSE 100 companies who attend our Audit Committee Institute events



Market share of the FTSE350 (YTD FY22)



FTSE350 audit bids won (YTD FY22)

02

## Investing in our audit business

100% 

Proportion of audit hours planned to be delivered using our new methodology and technology platform (KPMG Clara) for periods ending 31 December 2022

>£200m 

Cumulatively invested by KPMG in audit quality over the last 4 years

407  5% Partners and Directors

47%  2% Quality through diversity: Women

91%  3% Top talent retention

35%  0% Quality through diversity: BAME

111  59  
FY21 FY20

Upskilling our people  
Average number of hours of mandatory training

 449

Colleagues completing a professional qualification (e.g. ICAEW, ICAS)

03

## Measuring our progress

### External monitoring

Audit engagements rated 'good or limited improvement required' by the FRC's AQR in 2022

Audit engagements rated 'good or limited improvement required' by the ICAEW's QAD in 2022

91%  16%  
FTSE350

84%  25%  
All reviews

75%  25%  
Corporate

100%  0%  
Public Sector

Satisfactory rating in internal Quality Performance Reviews of audit engagements



### Employees responses in our Global People Survey to:

 81%

KPMG's commitment to quality is apparent in what we do on a day-to-day basis

 80%

I have access to the tools and resources I need to do my job effectively

 70%

I am satisfied with the learning and development available to improve my knowledge and skills

Note: changes to percentages are absolute not proportional

# Your digital audit – introducing KPMG Clara

To deliver a quality audit, not only do we need to understand your business and risks, we also need to implement market-leading technology. Technology is the core of our audit, assisting our risk assessment, delivering powerful data analytics and collaborating with management in real time on our audit. KPMG Clara is our global audit platform through which we plan, execute and manage the audit.

## Full transparency and real-time collaboration

Throughout the audit, management will have 24/7 access to the KPMG Clara collaboration portal and status of the audit. The technology provides easy access to key audit status information, including:

- How the audit is progressing.
- Tracking of engagement tasks.
- Finding out who from our KPMG team is leading on a deliverable.

A clear and transparent view on milestones, progress, and accountabilities facilitates direct collaboration with management.

## Globally efficient execution

At the core of the KPMG Clara workflow is a modern, intuitively written, easily applicable audit methodology, that coupled with our new functionality:

- Drives globally consistent and efficient execution.
- Enables early detection of issues so they can be quickly and effectively addressed.



## Insights-driven, efficient operations

Valuable insights help you better understand our independent audit assessment and should be relevant to the entity. Through KPMG Clara analytics, we are empowered to leverage the latest technologies, including data & analytics.

We use D&A to:

- Visualise the flow of transactions through your system.
- Identify risks in your financial data.
- Perform more specific audit procedures.

## Value from our transformative capabilities

We are committed to ensuring continuous improvement of the audit experience.

Our alliances with technology leaders such as Microsoft and IBM enable us to stay at the forefront of disruption and leverage our capabilities to deliver even more value through our audit.

With KPMG Clara, our relationship will be more impactful.

# Audit Scotland Code of Audit Practice

The Code of Audit Practice sets the framework for public audit in Scotland. It outlines the responsibilities of external auditors appointed by the Auditor General for Scotland and the Accounts Commission, and describes the scope of public audit in Scotland. This is set out on the following pages.

The Code of Audit Practice has refreshed the areas used to define the wider audit scope. The previous 2016 edition set out four areas (described as audit dimensions), i.e. financial management, financial sustainability, governance and transparency, and value for money. The new Code no longer uses the term audit dimensions, but it retains the areas of financial management and financial sustainability (though redefines each area) and replaces the other two as follows:

- governance and transparency dimension has been replaced with vision, leadership and governance area
- value for money dimension has been replaced with use of resources to improve outcomes.

Our audit will take the above areas into account in its execution.

## Responsibilities of management

### Financial Statements

Audited bodies must prepare an annual report and accounts containing financial statements and other related reports. They have responsibility for:

- preparing financial statements which give a true and fair view of their financial position and their expenditure and income, in accordance with the applicable financial reporting framework and relevant legislation;
- maintaining accounting records and working papers that have been prepared to an acceptable professional standard and that support their financial statements and related reports disclosures;
- ensuring the regularity of transactions, by putting in place systems of internal control to ensure that they are in accordance with the appropriate Council;
- maintaining proper accounting records; and
- preparing and publishing, along with their financial statements, an annual governance statement, management commentary (or equivalent) and a remuneration report that are consistent with the disclosures made in the financial statements. Management commentary should be fair, balanced and understandable and also clearly address the longer- term financial sustainability of the body.

Further, it is the responsibility of management of an audited body, with the oversight of those charged with governance, to communicate relevant information to users about the entity and its financial performance, including providing adequate disclosures in accordance with the applicable financial reporting framework. The relevant information should be communicated clearly and concisely.

Audited bodies are responsible for developing and implementing effective systems of internal control as well as financial, operational and compliance controls. These systems should support the achievement of their objectives and safeguard and secure value for money from the public funds at their disposal. They are also responsible for establishing effective and appropriate internal audit and risk-management functions.

Audited bodies are responsible for providing the auditor with access to all information relevant to the preparation of the financial statements, additional information requested and unrestricted access to persons within the entity.

# Audit Scotland Code of Audit Practice (continued)

## Responsibilities of management

### Prevention and detection of fraud and irregularities

Audited bodies are responsible for establishing arrangements for the prevention and detection of fraud, error and irregularities, bribery and corruption and also to ensure that their affairs are managed in accordance with proper standards of conduct by putting proper arrangements in place.

### Corporate governance arrangements

Each body, through its chief executive or accountable officer, is responsible for establishing arrangements to ensure the proper conduct of its affairs including the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. Audited bodies should involve those charged with governance (including Audit Committees or equivalent) in monitoring these arrangements.

### Financial position

Audited bodies are responsible for putting in place proper arrangements to ensure that their financial position is soundly based having regard to:

- such financial monitoring and reporting arrangements as may be specified;
- compliance with any statutory financial requirements and achievement of financial targets;
- balances and reserves, including strategies about levels and their future use;
- how they plan to deal with uncertainty in the medium and longer term; and
- the impact of planned future policies and foreseeable developments on their financial position.

### Best Value, use of resources and performance

The Scottish Public Finance Manual sets out that accountable officers appointed by the Principal Accountable Officer for the Scottish Administration have a specific responsibility to ensure that arrangements have been made to secure best value.

# Audit Scotland Code of Audit Practice (continued)

## Responsibilities of auditors

### Appointed auditor responsibilities

Auditor responsibilities are derived from statute, this Code, ISAs, professional requirements and best practice and cover their responsibilities when auditing financial statements and when discharging their wider scope responsibilities. These are to:

- undertake statutory duties, and comply with professional engagement and ethical standards;
- provide an opinion on audited bodies' financial statements and, where appropriate, the regularity of transactions;
- review and report on, as appropriate, other information such as annual governance statements, management commentaries, remuneration reports, grant claims and whole of government returns;
- notify the Auditor General when circumstances indicate that a statutory report may be required;
- participate in arrangements to cooperate and coordinate with other scrutiny bodies (local government sector only);
- demonstrate compliance with the wider public audit scope by reviewing and providing judgements and conclusions on the audited bodies:
  - effectiveness of performance management arrangements in driving economy, efficiency and effectiveness in the use of public money and assets;
  - suitability and effectiveness of corporate governance arrangements; and
  - financial position and arrangements for securing financial sustainability.

Weaknesses or risks identified by auditors are only those which have come to their attention during their normal audit work in accordance with the Code, and may not be all that exist. Communication by auditors of matters arising from the audit of the financial statements or of risks or weaknesses does not absolve management from its responsibility to address the issues raised and to maintain an adequate system of control.

This report communicates how we plan to identify, assess and obtain sufficient appropriate evidence regarding the risks of material misstatement of the financial statements due to fraud and to implement appropriate responses to fraud or suspected fraud identified during the audit.

# Audit Scotland Code of Audit Practice (continued)

## Responsibilities of auditors

### General principles

This Code is designed such that adherence to it will result in an audit that exhibits these principles.

### Independent

When undertaking audit work all auditors should be, and should be seen to be, independent. This means auditors should be objective, impartial and comply fully with the FRC ethical standards and any relevant professional or statutory guidance. Auditors will report in public and make recommendations on what they find without being influenced by fear or favour.

Our independence confirmation letter (page 16) discloses matters relating to our independence and objectivity including any relationships that may bear on the firm's independence and the integrity and objectivity of the audit engagement partner and audit staff.

We confirm that, in our professional judgement, KPMG LLP is independent within the meaning of regulatory and professional requirements and that the objectivity of the Director and audit staff is not impaired.

### Proportionate and risk based

Audit work should be proportionate and risk based. Auditors need to exercise professional scepticism and demonstrate that they understand the environment in which public policy and services operate. Work undertaken should be tailored to the circumstances of the audit and the audit risks identified. Audit findings and judgements made must be supported by appropriate levels of evidence and explanations. Auditors will draw on public bodies' self-assessment and self - evaluation evidence when assessing and identifying audit risk.

### Quality focused

Auditors should ensure that audits are conducted in a manner that will demonstrate that the relevant ethical and professional standards are complied with and that there are appropriate quality-control arrangements in place as required by statute and professional standards.



# Audit Scotland Code of Audit Practice (continued)

## Responsibilities of auditors

### Coordinated and integrated

It is important that auditors coordinate their work with internal audit, Audit Scotland, other external auditors and relevant scrutiny bodies to recognise the increasing integration of service delivery and partnership working within the public sector. This would help secure value for money by removing unnecessary duplication and also provide a clear programme of scrutiny activity for audited bodies.

### Public focussed

The work undertaken by external audit is carried out for the public, including their elected representatives, and in its interest. The use of public money means that public audit must be planned and undertaken from a wider perspective than in the private sector and include aspects of public stewardship and best value. It will also recognise that public bodies may operate and deliver services through partnerships, arm's-length external organisations (ALEOs) or other forms of joint working with other public, private or third sector bodies.

### Transparent

Auditors, when planning and reporting their work, should be clear about what, why and how they audit. To support transparency the main audit outputs should be of relevance to the public and focus on the significant issues arising from the audit.

### Adds value

It is important that auditors recognise the implications of their audit work, including their wider scope responsibilities, and that they clearly demonstrate that they add value or have an impact in the work that they do. This means that public audit should provide clear judgements and conclusions on how well the audited body has discharged its responsibilities and how well they have demonstrated the effectiveness of their arrangements. Auditors should make appropriate and proportionate recommendations for improvement where significant risks are identified.

# Restoring trust in audit and corporate governance

## Overview

- In May 2022, the Government released its response to the department of Business, Energy and Industrial Strategy (BEIS) white paper on Restoring Trust in Audit and Corporate Governance.
- They received over 600 responses.
- Proposals will be brought into force in variety of ways, including primary and secondary legislation, changes to Codes and Standards by the regulator and work by professional bodies.
- The timeline for legislation is unknown.

## A summary of the proposals

### Company & Directors

- Internal controls – changes to be introduced through the UK Corporate Governance Code, including an effectiveness statement on financial, operational and compliance internal controls systems.
- Fraud – reporting requirements that outline the steps taken by Directors to prevent and detect material fraud.
- A resilience statement – a short, medium and longer term view over the risks companies face, including one reverse stress.
- Dividend and capital maintenance – disclosure of topco distributable reserves, greater narrative disclosure of longer term capital maintenance and confirmation of legality of dividends.
- Audit and assurance policy – to set out different levels of assurance obtained over public financial and non-financial information.
- Audit Committee oversight – minimum standards to be introduced relating to the appointment and oversight of auditors, including allowing shareholders to consider the audit plan.

### Auditor

- Operational separation – required although largely achieved already voluntarily.
- Managed shared audits – on FTSE 350 entities, with powers available for ARGA to introduce a market cap in certain scenarios.
- Auditor education – to be enhanced for professional bodies.
- Enhancements to existing standards – to ensure that auditors take into account wider information in reaching their audit judgements.
- Engagement with shareholders – at AGMs and greater disclosure when auditors cease to hold office.

### Regulator

- New Public Interest Entity (PIE) definition – including private companies and LLPs with >750 employees and >£750m annual turnover.
- Strengthening the regulator – with the formation of ARGA with statutory powers, including:
  - over PIE directors for their corporate reporting and audit related responsibilities;
  - over professional accountancy bodies and their members.
- Reclaim powers from the RSBs – to register and approved auditors of PIEs.
- Actuarial profession and local public audits – will fall under ARGAs regulatory remit.



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