

1 The Brydon review of auditing (Lecture A669 – 10.34 minutes)

There has always been an 'expectation gap' where auditing is concerned. The expectation gap is the difference between what an audit actually is and what the auditor's responsibilities are and what users' *expect* the auditor to do. For example, when a corporate collapse occurs, the question that is frequently asked by non-accountants/auditors is '*why didn't the auditor's spot that?*' or '*what are the auditor's there to do?*'. On social media, there are often (incorrect) references by those who are not professionally trained in accounting/auditing to the auditor having a responsibility to detect fraud and even, in some cases, prevent fraud. ISA (UK) 240 *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements* is clear that the responsibility to prevent and detect fraud rests with management. Note, that the auditor is required to plan their work '*... to identify and assess the risks of material misstatement, whether due to fraud or error*' as set out in ISA (UK) 315 *Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment.*'

However, the fact still remains that the auditing profession has suffered immense setbacks over the last 12 months in the form of Carillion and Patisserie Valerie, to name two. Notwithstanding the fact that these two entities have suffered as a result of financial distress, whether the auditors were at fault remains to be seen and hence people should not be too quick to blame the auditors!

It is clear that the expectation gap is increasing and to address this, the Secretary of State for Business, Energy and Industrial Strategy (BEIS) has commissioned Sir Donald Brydon to carry out a review into the quality and effectiveness of audit. This review is expected to be completed by the end of 2019 from which a final report will be published and a Government consultation will be carried out on its response to the review's recommendations.

1.1 What will the review do?

The Government has said that the expectation gap is increasing. Audits focus on historical financial information and the financial position of the entity at its balance sheet date. The review aims to see what else the audit can do to respond effectively to the expectations of the users.

The review itself intends to take a 'fresh look' at the scope of audit and how far it can (and should) evolve to meet the needs of the financial statement users. In addition, the review will look at what other forms of assurance may be needed to help audit develop and to define and manage any residual expectations gap. The review intends to 'test' the current statutory audit model and ask whether it can be made more effective or whether change is required.

The review will take into consideration changing business models, new technology and the stronger public expectation.

1.2 What areas will be covered by the review?

The Government has said that the objectives of the review are 'ambitious' and the *Terms of Reference* includes six areas which will be covered (although these six areas are not exhaustive):

1. Understanding the needs and expectations of stakeholders who make use of company audits:
 - (a) the origins and perceptions of the expectations gap;
 - (b) what can be done to ensure that investors and other stakeholders fully engage with audit and understand its scope and limitations.
2. The scope of audit:
 - (a) what information future investors and the users of corporate information are likely to require a company to produce (drawing on the work of the FRC in this regard) and, in that context;
 - (b) what assurance investors and other users of corporate information will need; and
 - (c) how any extension of that assurance can be achieved at a proportionate cost to corporates.
3. How assurance is provided and how that assurance can be made more effective for investors:
 - (a) From whom and how the assurance should be provided;
 - (b) The extent to which auditors can and should assess whether underlying information is reliable;
 - (c) The extent to which auditors can and should assess the impact of uncertain future events; and
 - (d) How audit can respond to the opportunities and challenges of new technology and other forms of innovation to increase the assurance and effectiveness of audit.
4. How any change to the current statutory audit model will impact on potential liability of auditors.
5. How communication of audit findings to users can be improved to enable that information to be of more use.
6. The potential benefits and opportunities for international engagement and cohesion across the world on auditing standards.

The review has now called for views to help answer these and other questions.
You can find the review here:

<https://www.gov.uk/government/consultations/the-quality-and-effectiveness-of-audit-call-for-views>