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June 2021

Quoted Companies Alliance

BEIS audit reform consultation

QUOTED COMPANIES ALLIANCE

Methodology

What?	**20 minute online survey**
Who?	**166 x small-mid cap companies** **52 x institutional investors**
When?	**10th May – 2nd June 2021**

Executive summary

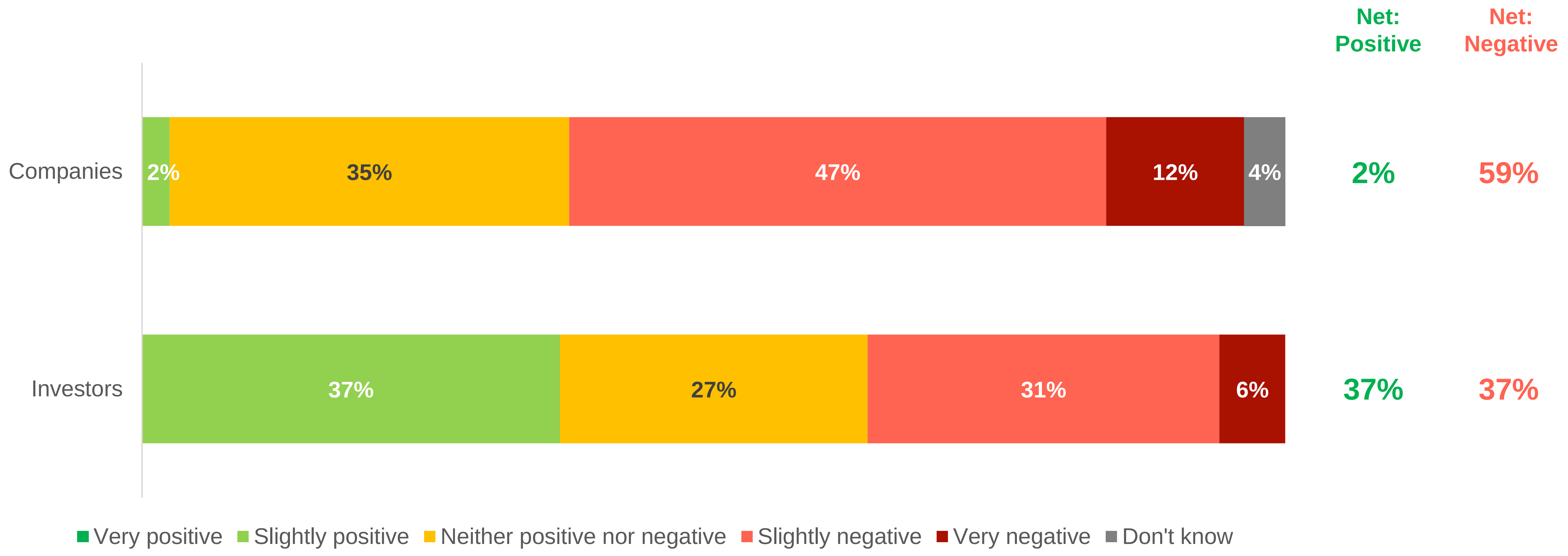
- Having read through the proposals, three-fifths of companies believe that if the proposed reforms are implemented unchanged, there will be a negative impact on their growth.
- Nine-tenths of companies and four-fifths of investors believe the proposals have the potential to deter prospective individuals from becoming directors of publicly quoted companies.
- Both companies and investors believe the proposed reforms will lead to companies' boards spending more time on compliance matters. While companies estimate compliance currently takes around a third of board time, the new proposals would mean compliance taking around half of board time.
- Nine-tenths of respondents agree the proposed phased introduction of the requirements should be paused in order to conduct a comprehensive analysis of the impact of the reforms.
- The majority of respondents, both investors and companies, believe the current state of enforcement is effective in deterring malpractice.
- A third of companies believe the reforms will have a negative effect on the level of confidence that the UK is an attractive listing venue, although investors are more likely to believe there will be a positive effect.

General questions – Impact

Around six in every ten companies expect a negative effect on their growth if the reforms are implemented

Over six in every ten investors do not foresee a positive effect on company growth

If the proposed reforms are implemented unchanged, what impact, if any, do you believe it will have on your company's growth?



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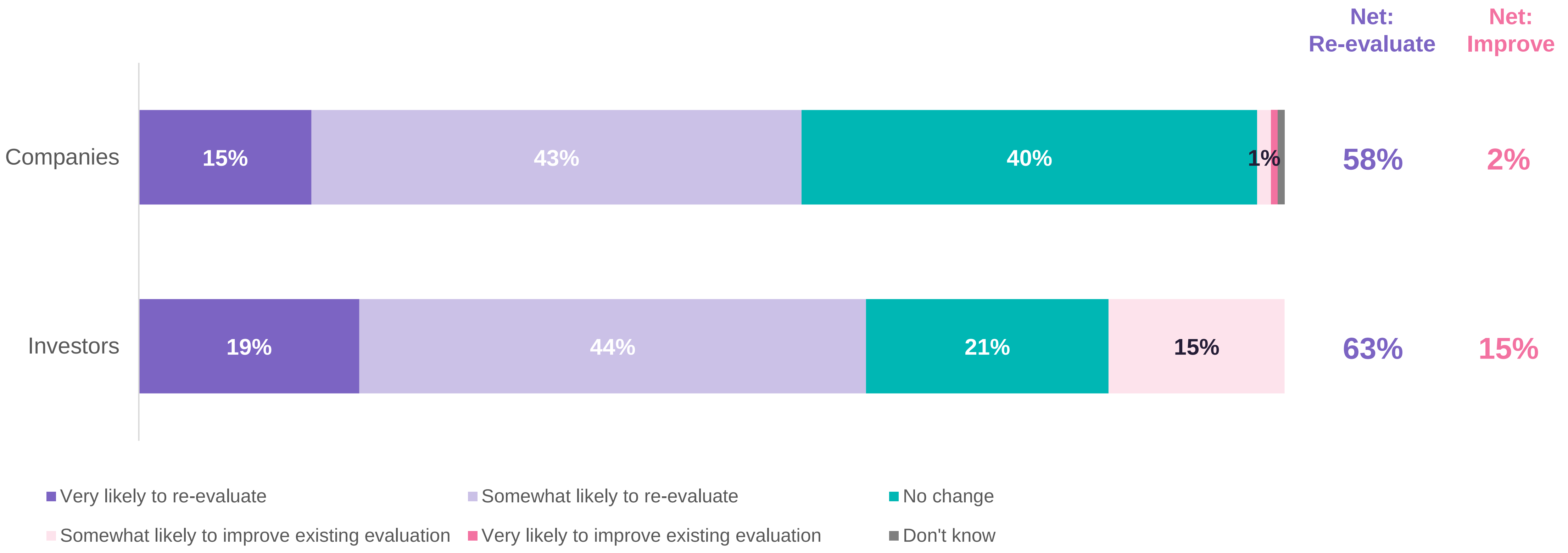
*Wording for investors: If the proposed reforms are implemented unchanged, what impact, if any, do you believe it will have on companies' growth?

Base: all respondents (218); companies (166); investors (52)

Around six in every ten companies say the proposed reforms would likely lead them to re-evaluate the worthwhileness of a company listing on a public market. Investors hold the same strength of view

If implemented, to what extent, if at all, could the proposed reforms impact your evaluation of the worthwhileness of your company's listing/quotation on a public market?



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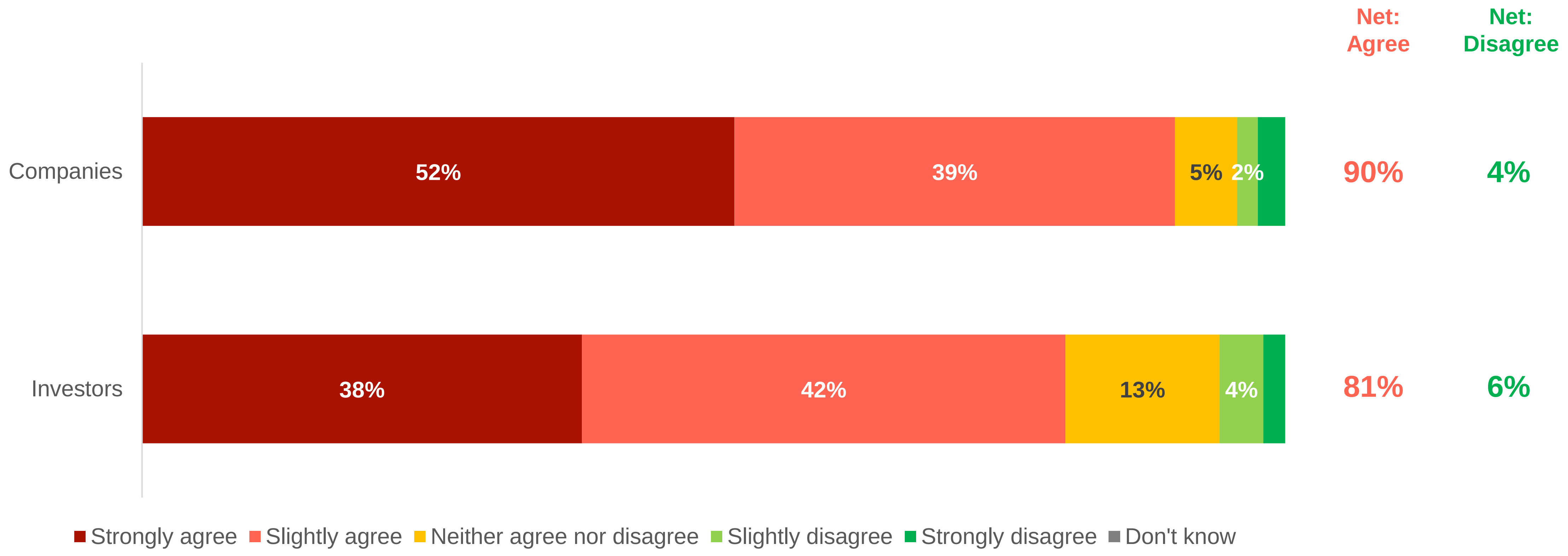
QUOTED COMPANIES ALLIANCE

*Wording for investors: If implemented, to what extent, if at all, could the proposed reforms impact your evaluation of the worthwhileness of a company's listing/quotation on a public market?
Base: all respondents (218); companies (166); investors (52)

Nine in ten companies, and eight in ten investors, agree the reforms have the potential to deter individuals from becoming directors of publicly listed companies

To what extent, if at all, do you agree or disagree that these proposals have the potential to deter prospective individuals from becoming directors of publicly quoted companies, or existing directors from retaining their position as a director of a publicly quoted company?



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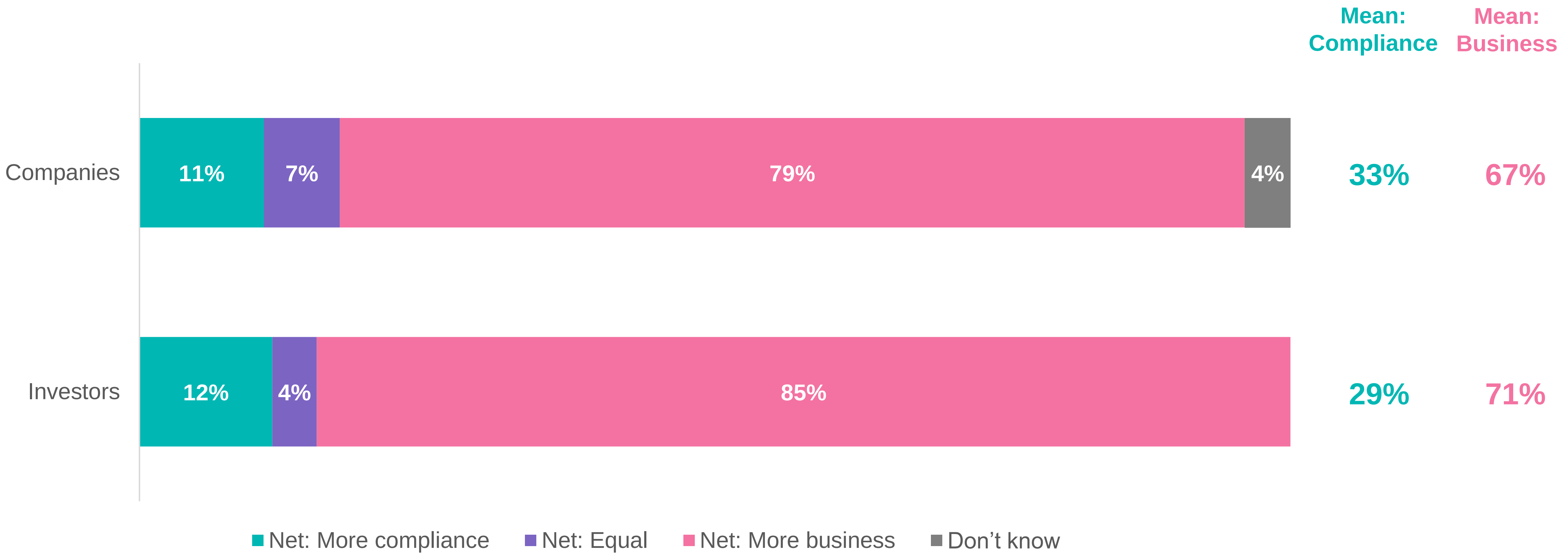
Base: all respondents (218); companies (166); investors (52)

On average, companies say they spend a third of time on compliance

Investors have a similar view when asked how much time they envision companies currently spend on compliance

As a ratio, how much time does your board currently spend on governance/compliance matters as opposed to business/growth/future planning matters?*



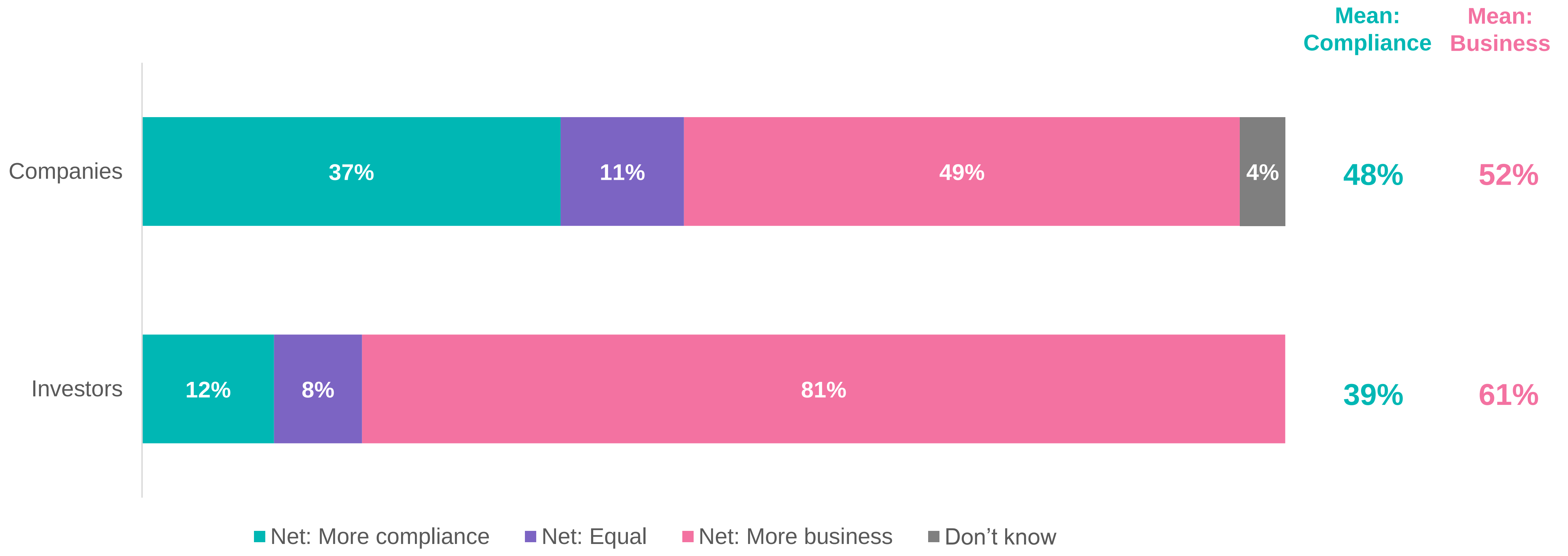
*Wording for investors: “*As a ratio, how much time do you envisage a company currently spends on governance/compliance matters as opposed to business/growth/future planning matters?*”

Base: all respondents (218); companies (166); investors (52)

The expectation among both audiences is that the proportion of time spent on compliance will increase if the reforms are implemented unchanged

Investors do, however, anticipate more time being spent on business than the companies themselves do

If the reforms are implemented unchanged, how much time, as a ratio, do you expect your board will spend on governance/compliance matters as opposed to business/growth/future planning matters?*



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*Wording for investors: If the reforms are implemented unchanged, how much time, as a ratio, do you expect a company will spend on governance/compliance matters as opposed to business/growth/future planning matters?

Base: all respondents (218); companies (166); investors (52)

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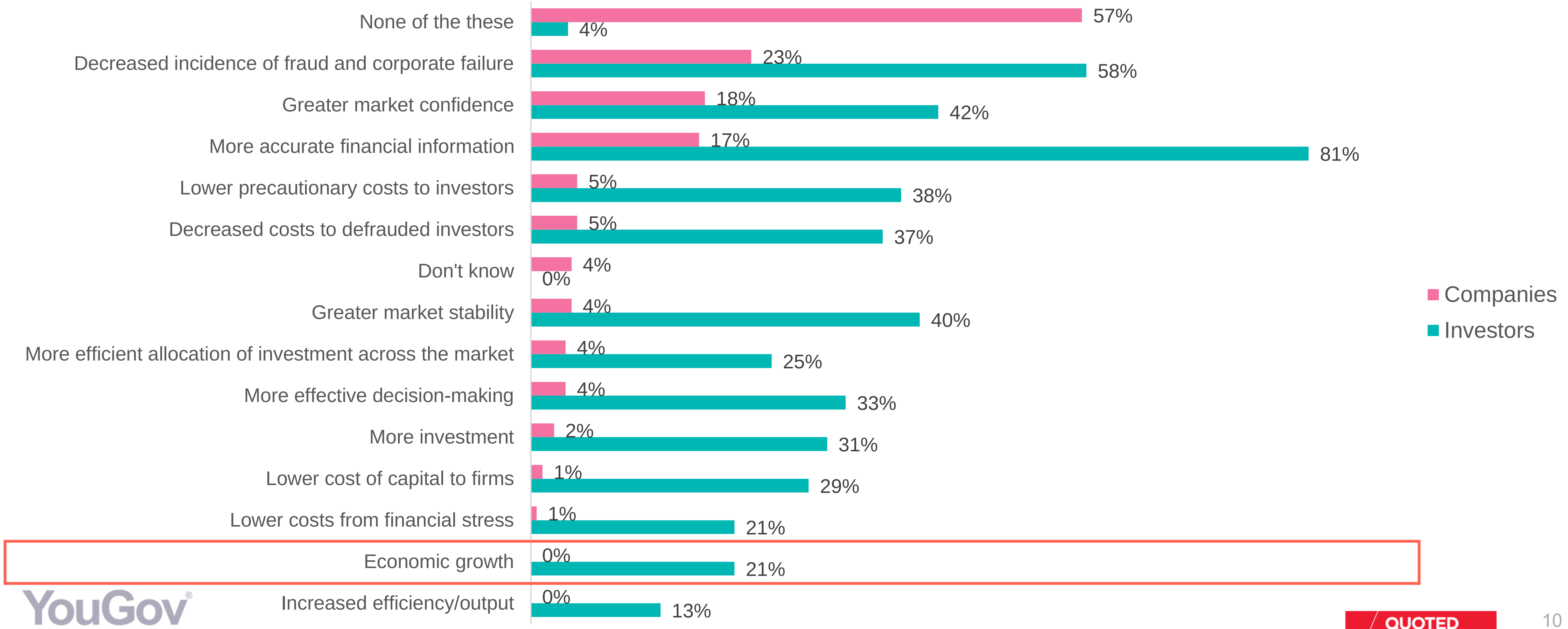
Almost three in five company respondents do not anticipate the proposals leading to any of the listed benefits, and not one company expects economic growth

Four-fifths of investors, however, think there will be more accurate financial information

In your opinion, do you believe that the proposals outlined in the consultation will lead to any of the following?

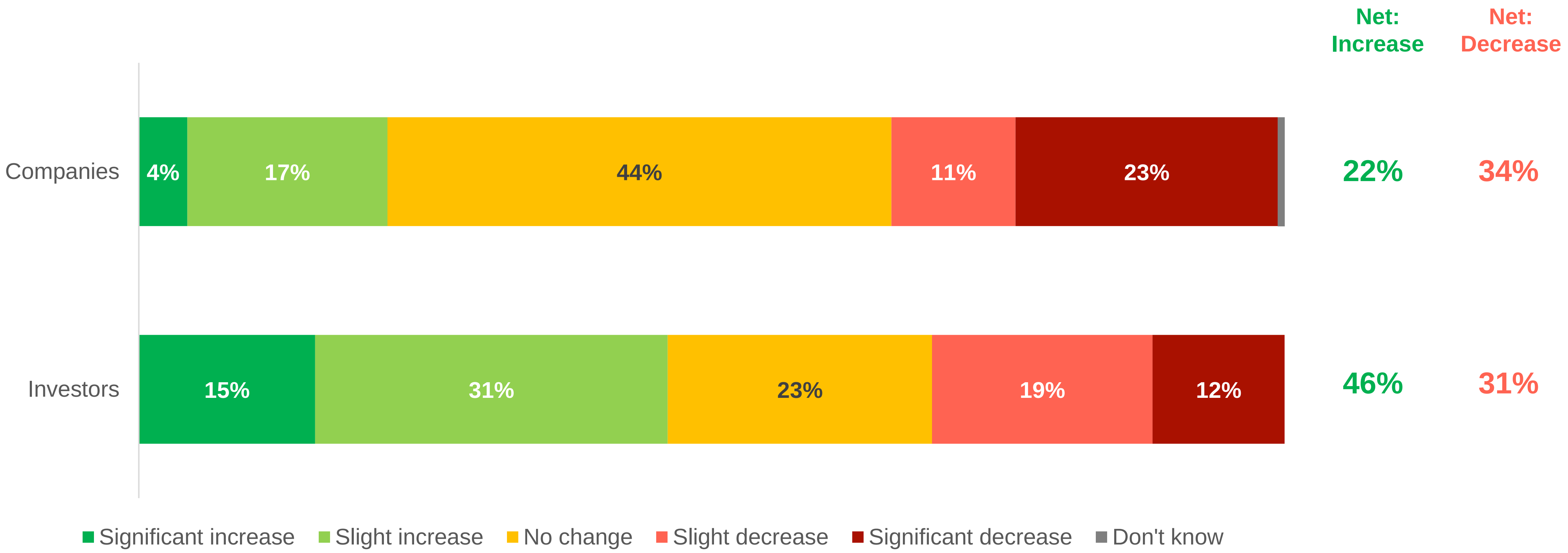


Base: all respondents (218); companies (166); investors (52)

Over a third of companies expect the proposed reforms to decrease the level of confidence in the UK as a listing venue

Over half of investors do not anticipate an increase in confidence

To what extent, if at all, do you think the proposed reforms will have an impact on the level of confidence that the UK is an attractive listing venue?



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Base: all respondents (218); companies (166); investors (52)

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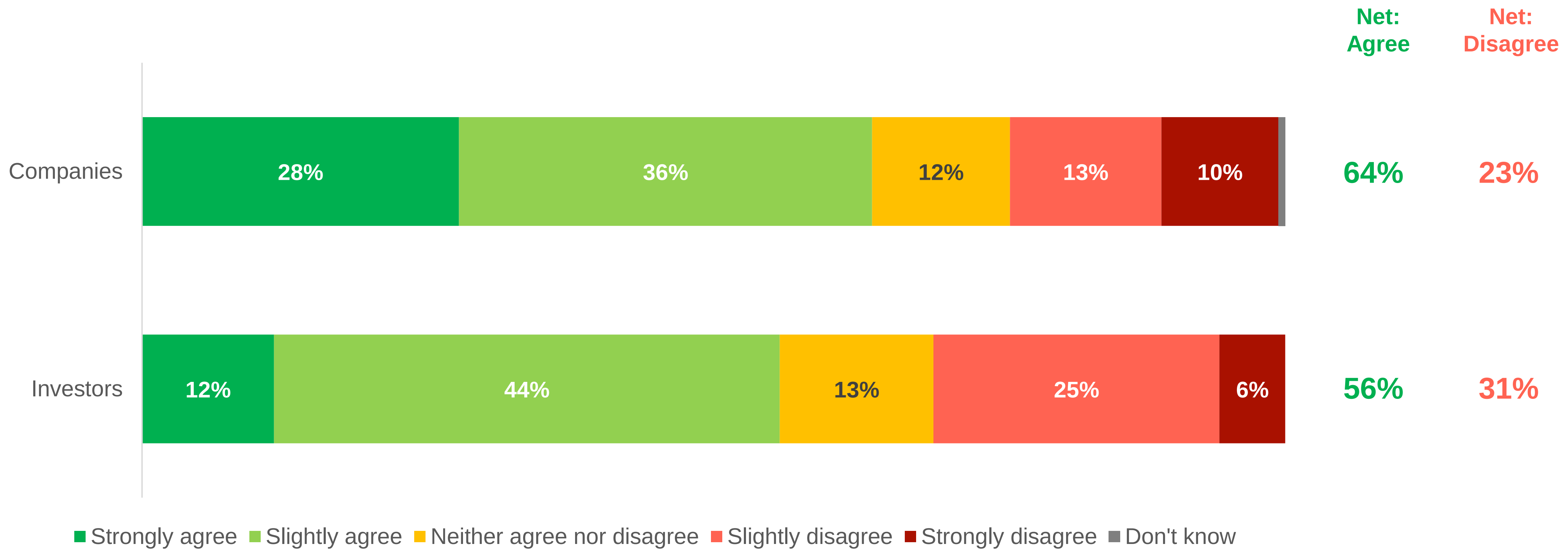
Around two-thirds of companies and over half of investors believe the current state of enforcement is effective at deterring malpractice

Almost quarter of companies and a three-tenths of investors think it ineffective, however

To what extent, if at all, do you agree or disagree that the current state of enforcement is effective in deterring malpractice such as fraud and criminal negligence?

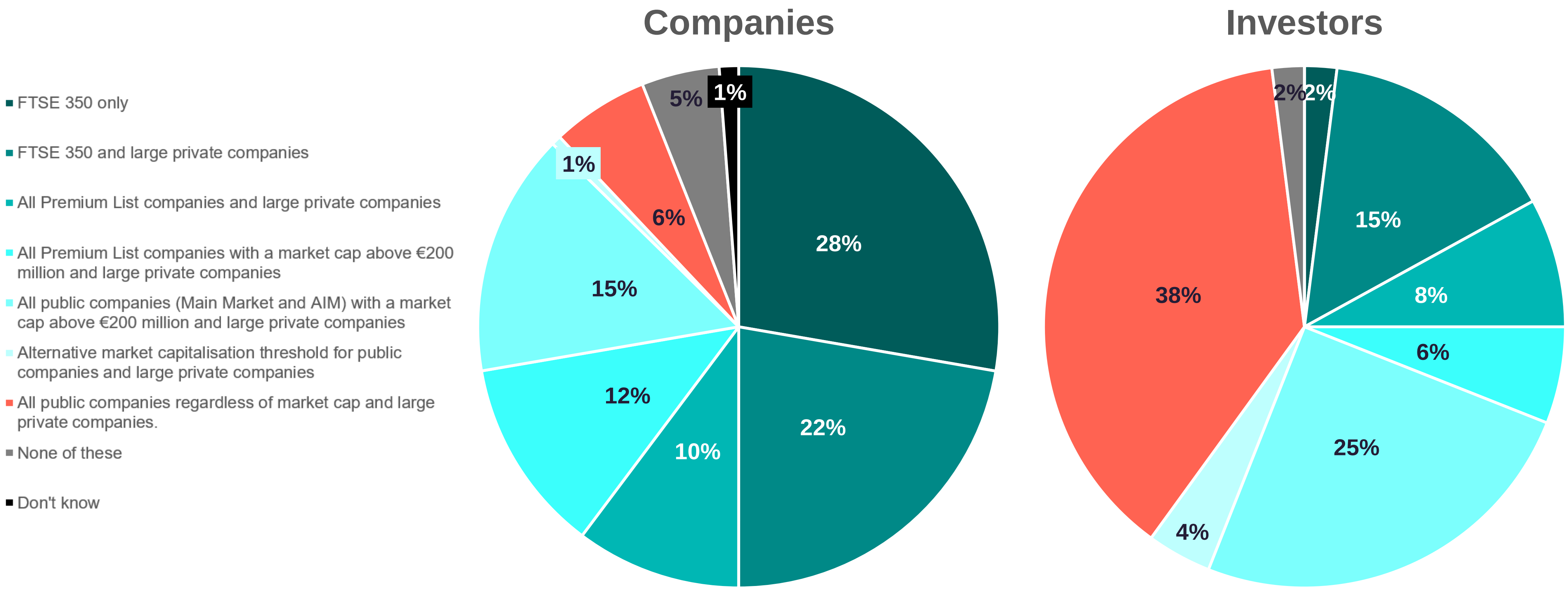


Base: all respondents (218); companies (166); investors (52)

General questions - Implementation

Three in every five investors would like to see a delineated approach to determining which are the appropriate companies to target for these reforms. Nine in every ten companies agree with this approach

The stated purpose of the reforms is to improve the level of information provided and increase confidence in UK companies. In your opinion, which are the appropriate companies that should be the target of the reforms?

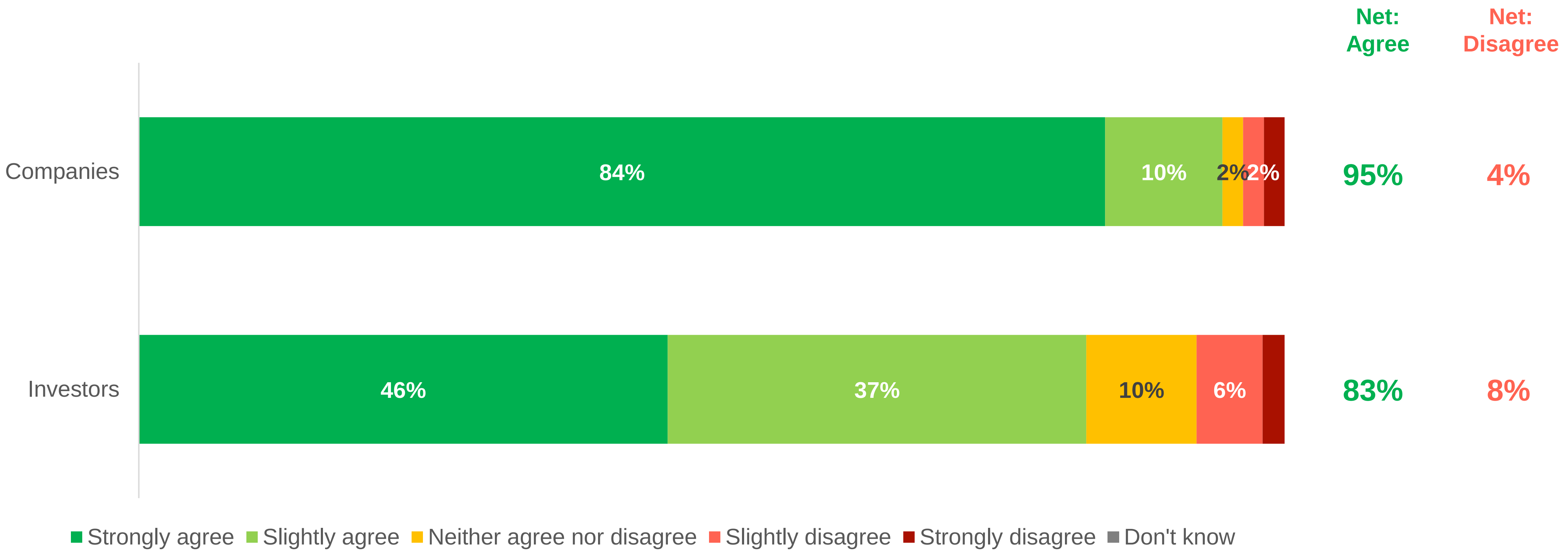


Base: all respondents (218); companies (166); investors (52)

The vast majority of respondents agree there should be a pause for a comprehensive analysis of the impact of the reforms

Over nine in ten companies and over eight in ten investors agree

If the reforms are implemented for the highest profile companies, to what extent, if at all, do you agree or disagree that there should be a pause in order to conduct a comprehensive analysis of the impact of the reforms before consideration is given to extending the requirements to other entities, such as those on AIM?



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QUOTED COMPANIES ALLIANCE

Base: all respondents (218); companies (166); investors (52)

Areas of reform

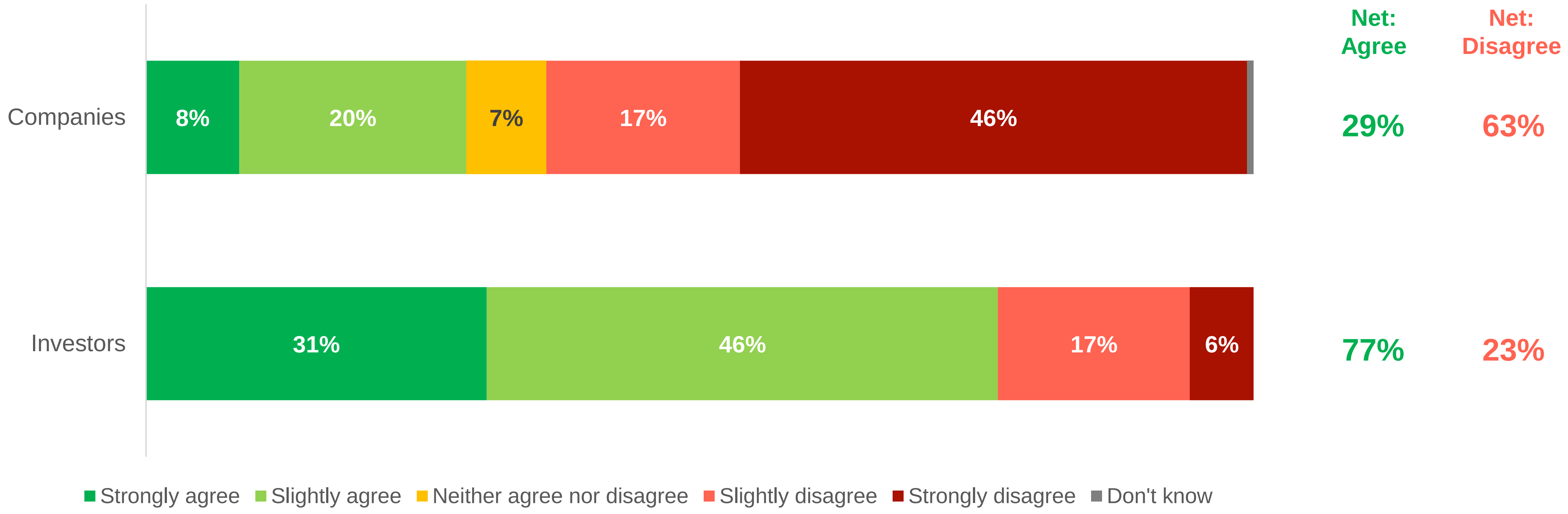
Expanding the definition of a Public Interest Entity (PIE)

Proposal: To extend the definition of a PIE to include large private companies and large AIM-quoted companies with a market capitalisation above €200 million. The Government is considering that a company will be required to meet the threshold for three consecutive financial years, as well as considering a phased introduction. The definition would currently capture approximately 105 AIM companies. However, this is likely to increase as companies grow. All companies on the Main Market, irrespective of their size, will be in scope.

The total cost is estimated by the Government to be up to £1.7 billion for the entities captured over a 10-year period. The costs for companies, and indirectly for investors, are expected to arise from, amongst other things: familiarisation costs for the PIE regime mandatory retendering and audit rotation exercise costs and compliance costs from additional regulatory reporting requirements.

Three in every four investors agree AIM companies with a market cap over €200m should be included in the definition, however six in every ten companies disagree

To what extent, if at all, do you agree or disagree that all AIM companies with a market cap above €200 million should be included in the definition?

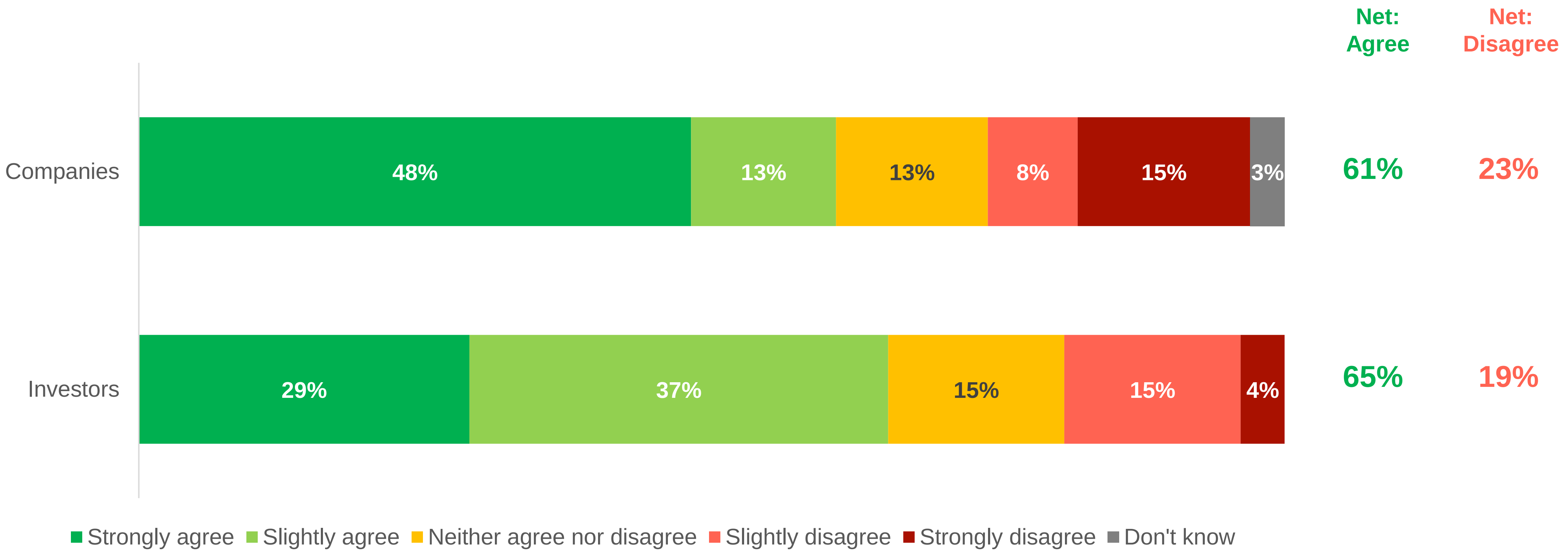


Full wording: The Government's objective is to introduce a wider definition of public interest entity to ensure large businesses that are of public importance are subject to appropriate regulation. To what extent, if at all, do you agree or disagree that all AIM companies with a market cap above €200 million should be included in the definition?

Base: all respondents (218); companies (166); investors (52)

But both companies and investors generally agree if the €200m threshold is taken forward, it should also be applied to companies on the Main Market

If the €200 million market capitalisation threshold for AIM companies is taken forward, do you agree or disagree this threshold should also be applied to companies on the Main Market?



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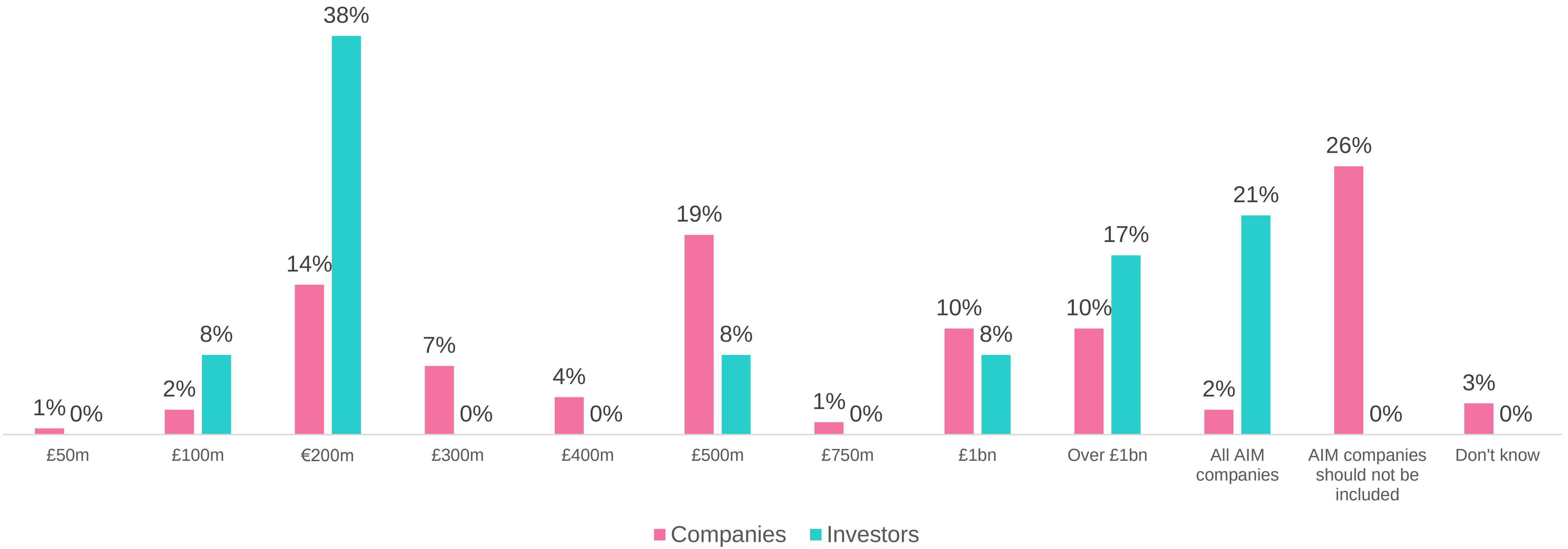
Base: all respondents (218); companies (166); investors (52)

Companies are most likely to say AIM companies should not be included. Investors are most likely to say that a threshold of €200m is appropriate for the expanded PIE definition

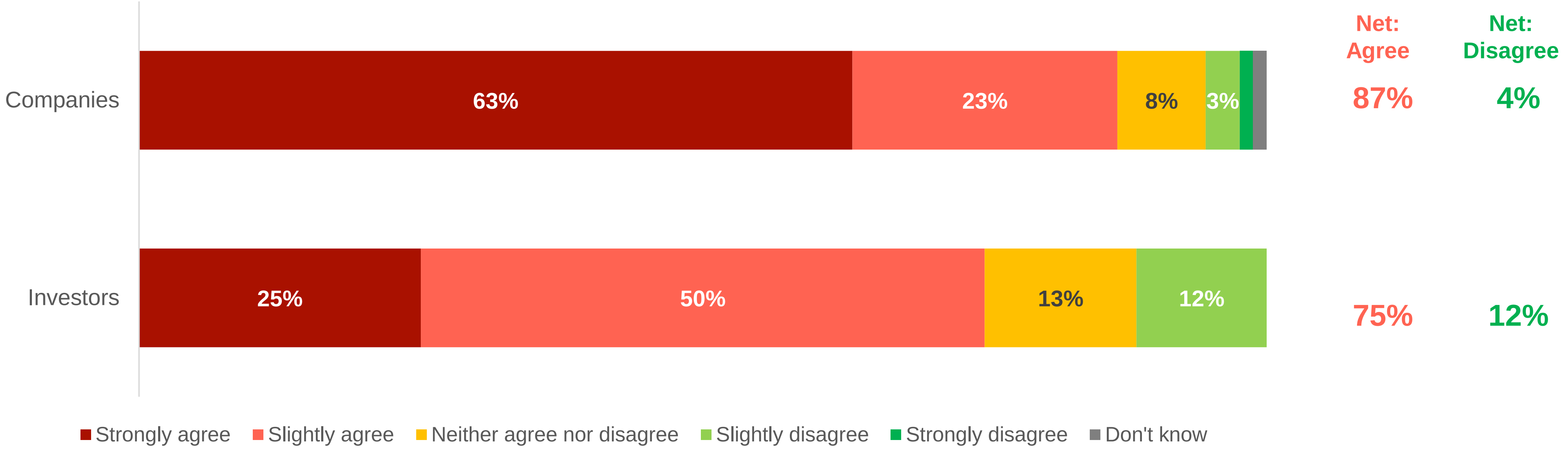
What is the appropriate market capitalisation threshold for companies on AIM to be included in the expanded PIE definition?



*the Government's proposal of €200m is stated in Euros (€) due to the thresholds origins in the EU
Base: all respondents (218); companies (166); investors (52)

But the vast majority of both companies and investors agree the proposed expansion of the PIE definition will be too onerous

To what extent, if at all, do you agree or disagree that the proposed expansion of the PIE definition will be too onerous/costly?



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Base: all respondents (218); companies (166); investors (52)

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Introducing a strengthened regime for internal controls

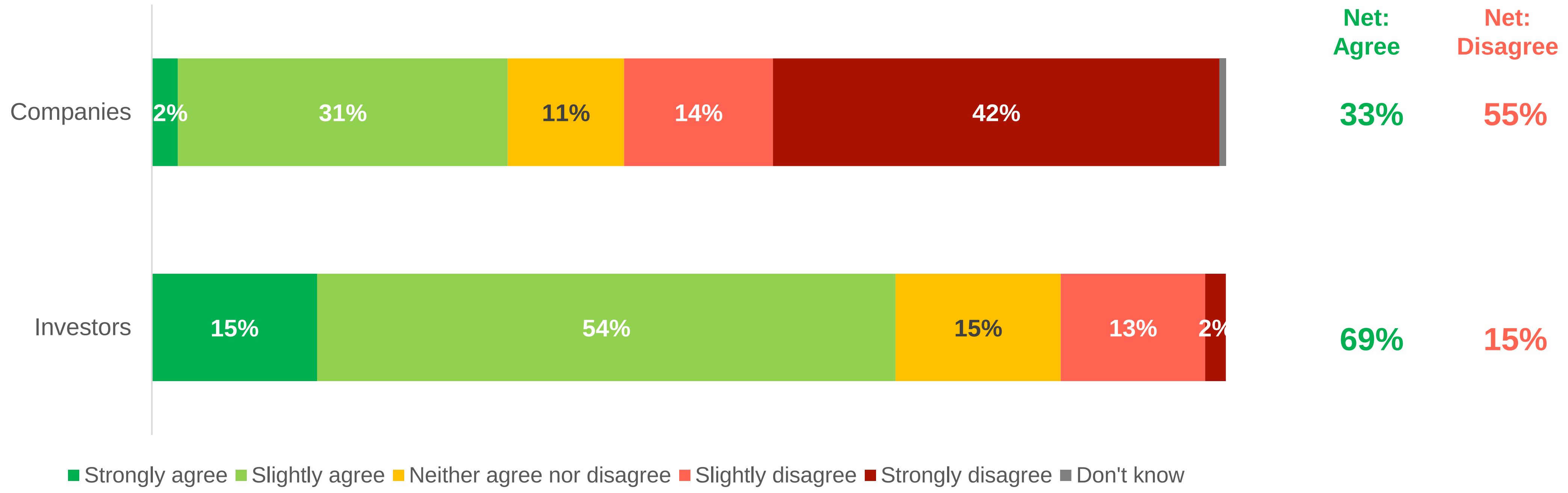
Proposal: The Government is considering applying several options on internal controls to PIEs to address high profile company failures:

1. **Option 1** requires an explicit directors' statement about the effectiveness of the internal control and risk management systems.
2. **Option 2** is Option 1 + the requirement for auditors to report more about their views on the effectiveness of companies' internal control systems.
3. **Option 3** is Option 1 + the requirement for auditors to express a formal opinion on the directors' assessment of the effectiveness of the internal control systems.

The government estimates the total cost over a 10-year period will be £1.452 billion (Option 1); £1.459 billion (Option 2); or £2.322 billion (Option 3). The costs for companies, and indirectly for investors, would arise through additional compliance costs and investment in new internal financial reporting systems. In addition, audit fees are expected to rise in Options 2 and 3, with an estimated increase of 5-35% for Option 3.

The majority of investors agree the attestation proposal will reduce the number of frauds, although the majority of companies disagree

To what extent, if at all, do you agree or disagree that the proposal to implement an attestation on certain internal controls will effectively address these concerns and reduce the number of intentional inaccuracies/frauds?

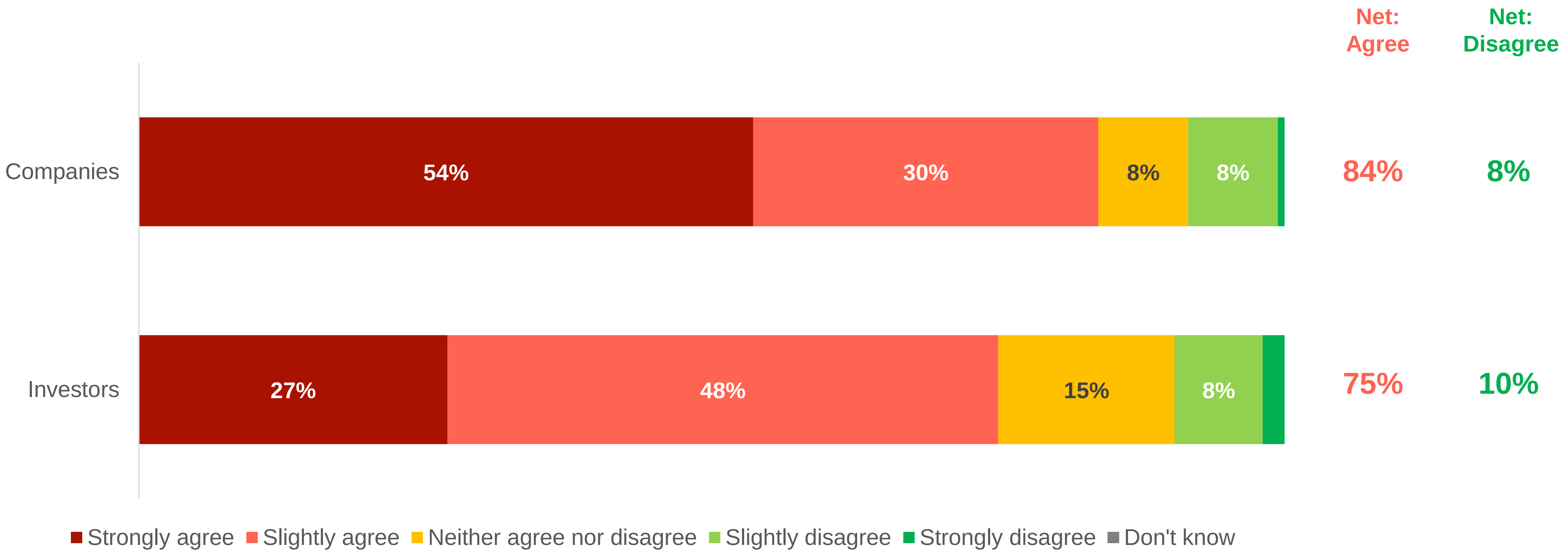


Full wording: The Government is seeking to address "high-profile firm failures where weak internal controls and poor risk management have eroded confidence". To what extent, if at all, do you agree or disagree that the proposal to implement an attestation on certain internal controls will effectively address these concerns and reduce the number of intentional inaccuracies/frauds?

Base: all respondents (218); companies (166); investors (52)

The majority of both companies and investors are agreed that changes to the internal controls framework will be too costly and will disincentivise individuals from taking on responsibility

To what extent, if at all, do you agree or disagree the proposed changes to the internal controls framework will be too onerous/costly and disincentivise individuals from taking on that responsibility and associated liability?



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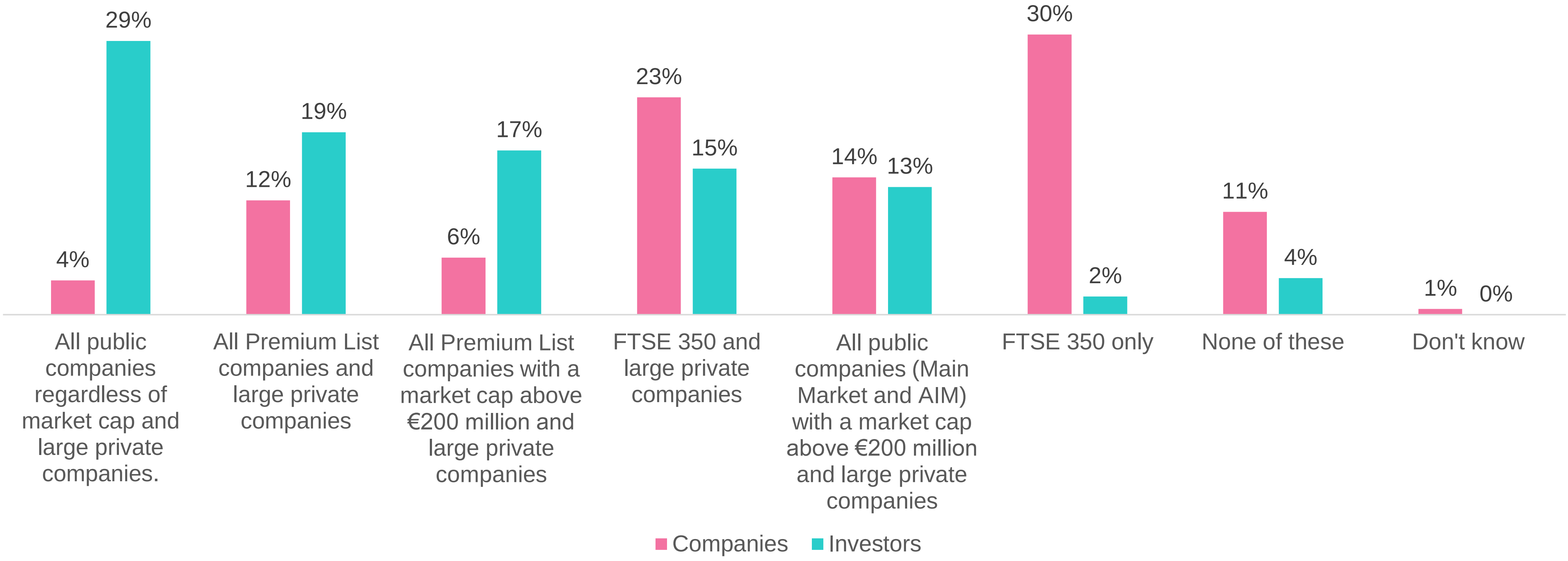
Base: all respondents (218); companies (166); investors (52)

Over half of companies think the reforms should be targeted at either FTSE350 only or FTSE350 and large private companies. Three in every five investors would like to see some sort of delineated approach to determining the appropriate companies to target.

In your opinion, where should the proposed reforms to internal controls be targeted?



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Base: all respondents (218); companies (166); investors (52)

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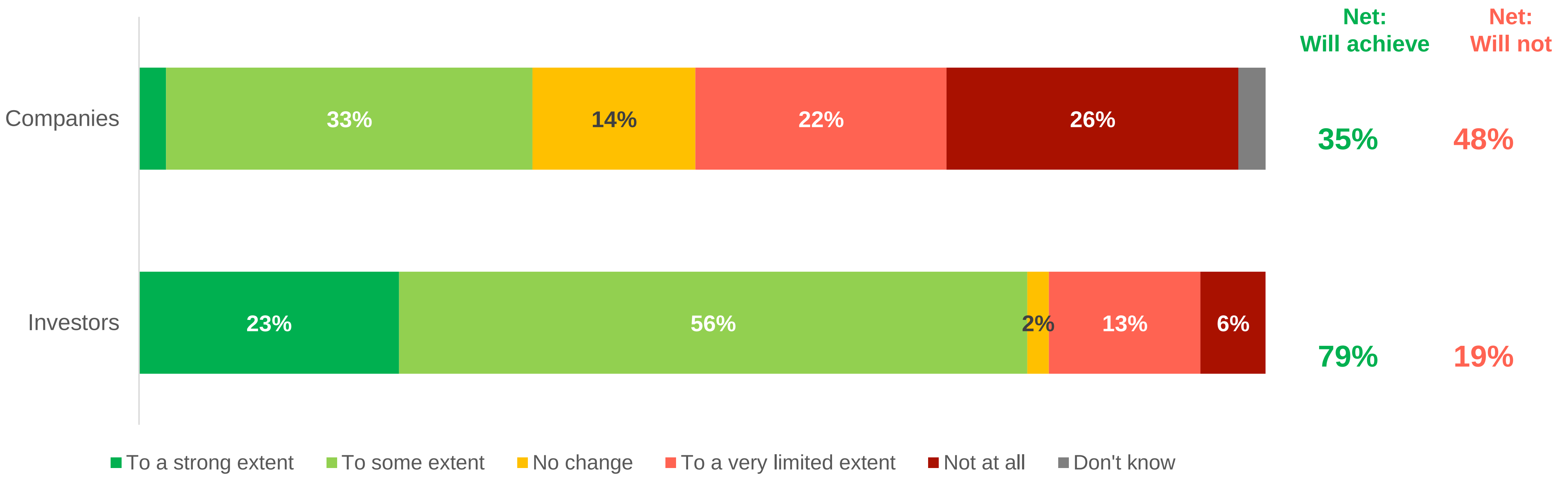
New corporate reporting requirements

Proposal: To introduce a requirement for PIEs to produce an annual Resilience Statement that consolidates and builds upon existing going concern and viability statements and an annual Audit and Assurance Policy, which would describe the company's approach to seeking assurance of its reported information. These will be required of Premium List companies first and extended to all other PIEs two years later.

The maximum total cost estimated by the government of the Resilience Statement and Audit and Assurance Policy for all entities over a 10-year period is £8.4m and £26.8 million respectively. Companies in scope would also face familiarisation costs.

While eight in every ten investors believe the proposals will lead to greater evidence of resilience from directors, companies are generally more likely to think they will not

The Government believes directors should do more to evidence plans to maintain resilience and explain their approach to seeking assurance of key business information and processes. To what extent do you believe that the proposals will achieve this?



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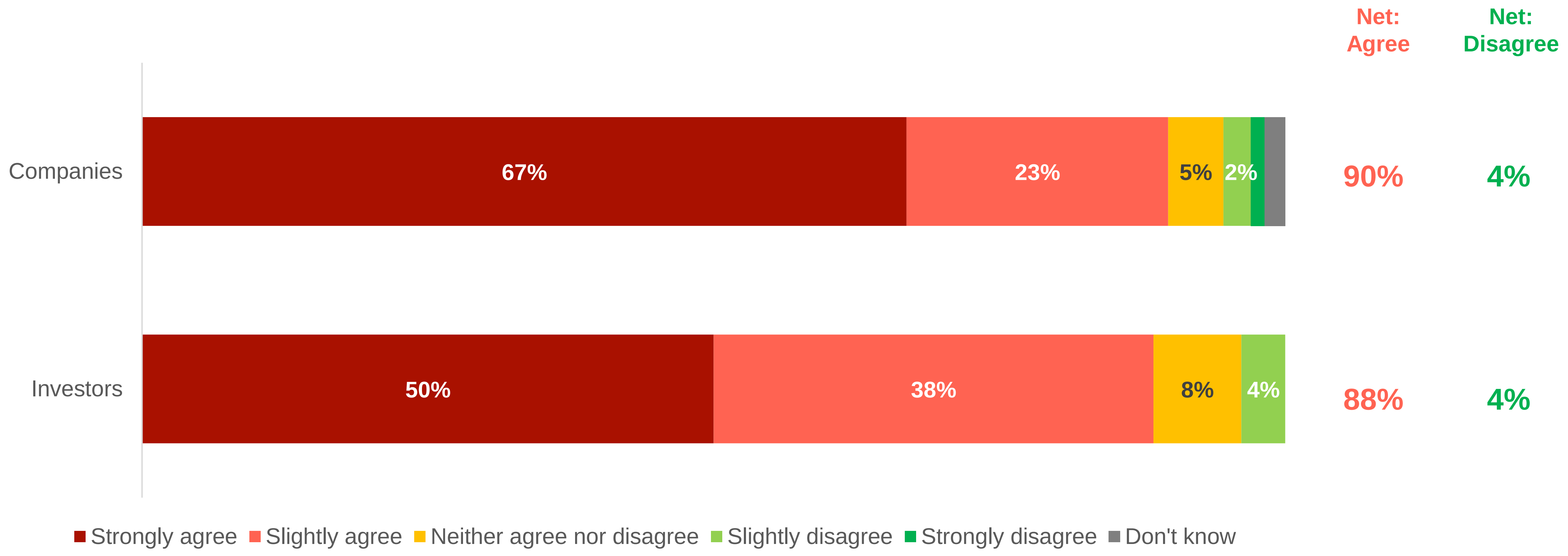
QUOTED COMPANIES ALLIANCE

Base: all respondents (218); companies (166); investors (52)

Around nine in ten of both companies and investors agree the Audit and Assurance Policy will lead to boilerplate statements

To what extent, if at all, do you believe that the Audit and Assurance Policy will lead to boilerplate statements (i.e. standardised statements that change little year-on-year)?



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QUOTED COMPANIES ALLIANCE

Base: all respondents (218); companies (166); investors (52)

Greater enforcement against company directors

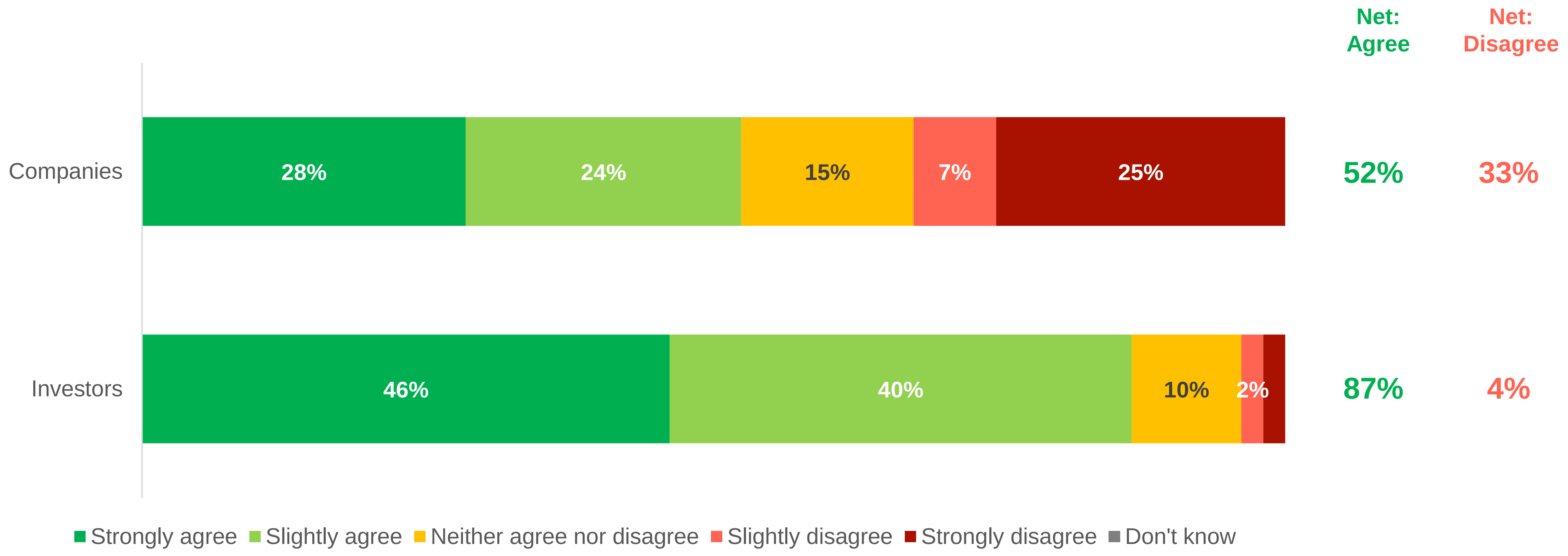
Proposal: To give the regulator increased powers to hold all directors of PIEs to account (not just chartered accountants), allowing the regulator to take action against breaches of corporate reporting and audit-related responsibilities, as well as a regime that gives further attention to malus and clawback provisions in remuneration arrangements.

The monetised costs are expected to be incurred by the regulator and business as follows: Enforcement regime for directors that are not chartered accountants (Regulator £0.2m non-recurrent cost and £5.3m recurrent cost, Business £3.5m recurrent cost); and Power to investigate directors and refer to insolvency service (Regulator £0.1m non-recurrent cost and £2.6m recurrent cost). The changes to the malus and clawback regime have not yet been costed.

The vast majority of investors agree with the proposal to extend regulator powers to take action against all directors

Companies are generally more likely to agree with this too, although a third disagree with it

To what extent, if at all, do you agree or disagree with the proposal to extend the powers of the regulator to be able to take action for breaches on existing corporate reporting and audit duties against all directors and not just chartered accountants?



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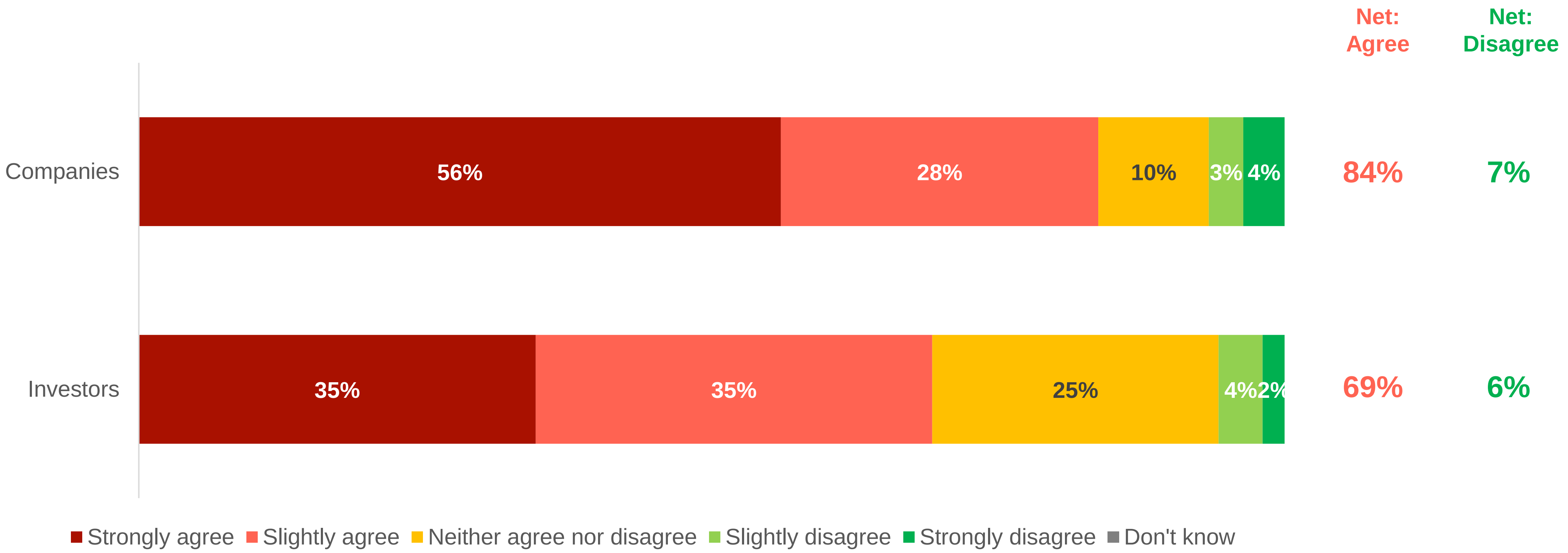
QUOTED COMPANIES ALLIANCE

Base: all respondents (218); companies (166); investors (52)

The majority of both companies and investors believe the proposals could deter individuals from becoming or remaining directors of publicly quoted companies

To what extent, if at all, do you agree or disagree that these proposals have the potential to deter prospective individuals from becoming directors of publicly quoted companies, or existing directors from retaining their position as a director of a publicly quoted company?



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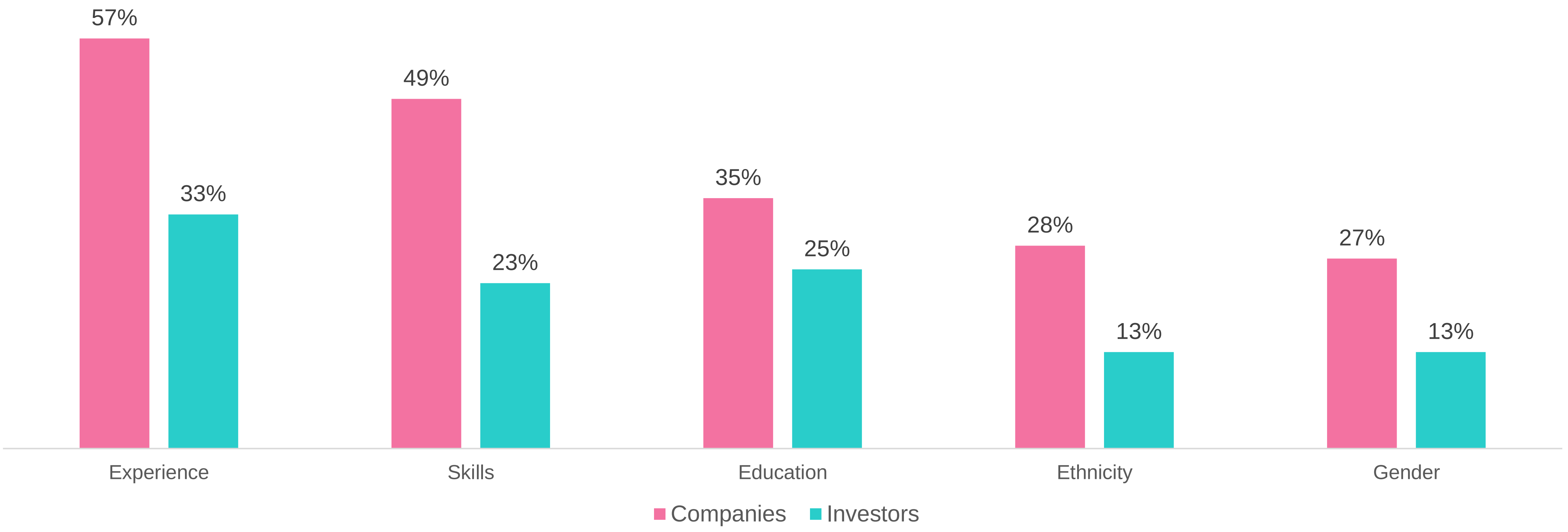
QUOTED COMPANIES ALLIANCE

Base: all respondents (218); companies (166); investors (52)

Companies believe increasing enforcement against directors will most negatively impact board diversity in terms of experience and skills

Investors are also most likely to anticipate impacts on experience and education

In your opinion, do you believe that increasing enforcement against directors will negatively impact board diversity in terms of any of the following?



Base: all respondents (218); companies (166); investors (52)

Audit purpose and scope

Proposal: To change the purpose and scope of audit to help tackle fraud by:

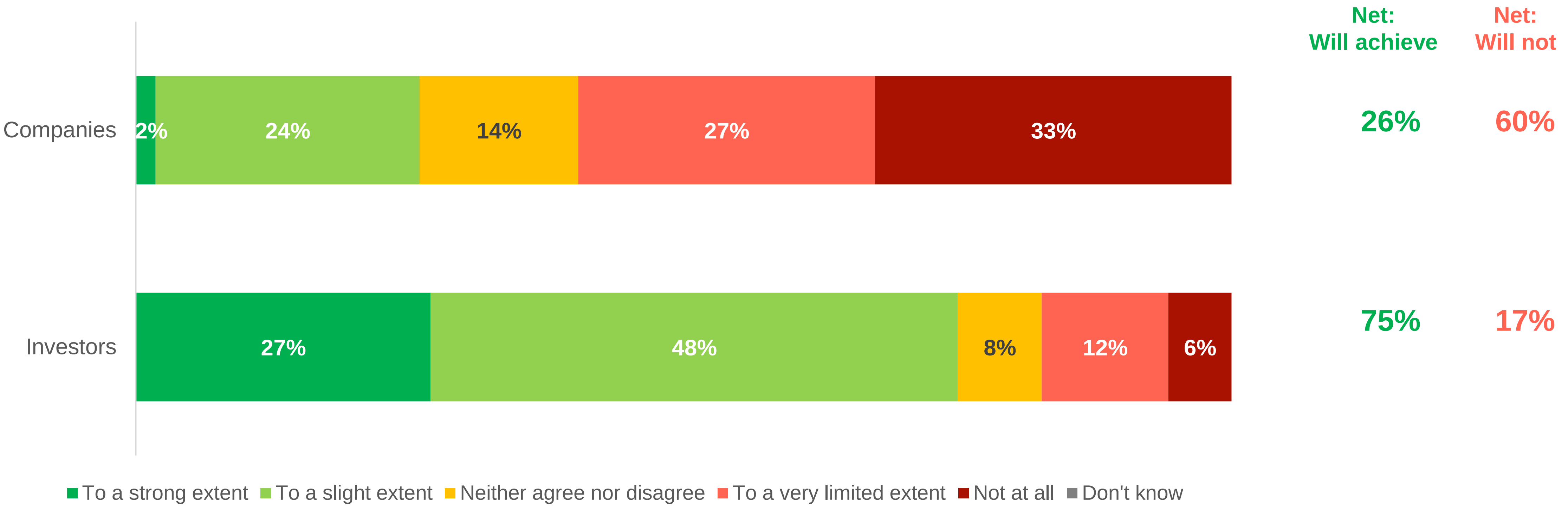
1. **Option 1** will require directors to issue a statement outlining the actions taken to prevent and detect material fraud.

2. **Option 2** is Option 1 + a requirement for auditors to report on the directors' statement.

The total estimated cost by the government for the entities in scope over a 10-year period is estimated to be £7.1m (Option 1); or £13.2m (Option 2).

Three-quarters of investors believe the proposals will lead to an increase in public confidence, although only a quarter of companies think the same

The Government seeks to provide greater clarity regarding the respective roles of directors and auditors, to restore public confidence. To what extent do you believe the proposals will lead to an increase in public confidence and a marked improvement in the detection and prevention of fraud?



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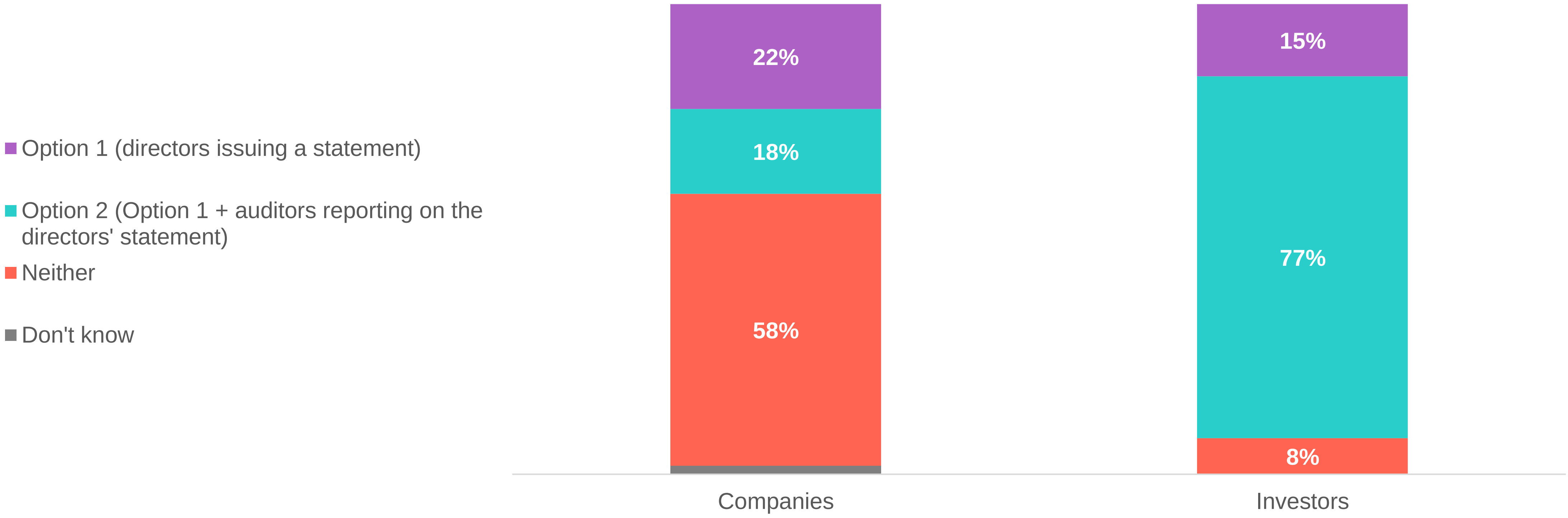
QUOTED COMPANIES ALLIANCE

Base: all respondents (218); companies (166); investors (52)

Over three-quarters of investors would prefer to see option 2 implemented. Of the two, companies are more likely to opt for option 1, but the majority would prefer neither

What is your preferred option?



Base: all respondents (218); companies (166); investors (52)

Increased Audit Committee oversight and engagement with shareholders

Proposal: The Government is considering three options regarding audit committee oversight:

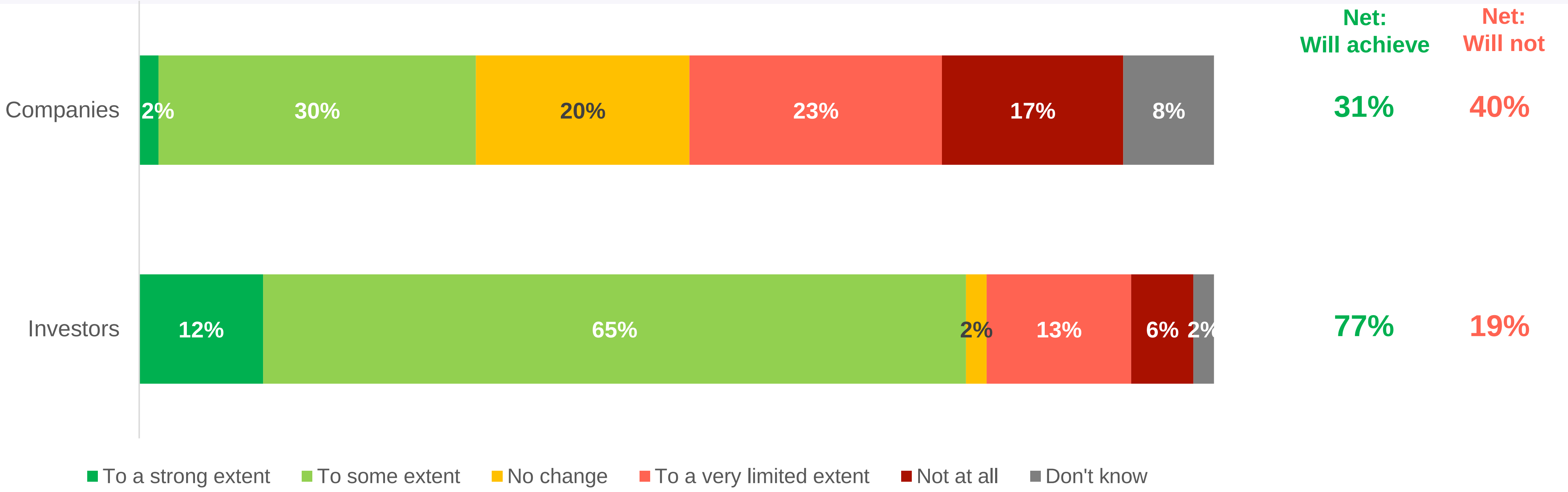
1. **Option 1** is concerned with mandating, monitoring and enforcing minimum standards for audit committee activities, including: tendering (for the appointment of a new auditor), oversight and reporting for ALL FTSE 350 audit committees.
2. **Option 2** is concerned with mandating, monitoring and enforcing minimum standards for audit committee activities, including: tendering (for the appointment of a new auditor), oversight and reporting, using a risk-based monitoring approach.
3. **Option 3** is concerned with using a non-mandatory standard for tendering, oversight and reporting, with a "comply or explain" approach.

The requirements will apply to FTSE 350 audit committees; however, the Government will retain the option to extend to a wider scope of PIEs. The Government's total estimated cost of the new requirements, related to audit committee oversight for the entities in scope over a 10-year period is estimated to be £72.5m (Option 1); £12m (Option 2); or £1.4m (Option 3). Audit committees would face costs from increased regulatory oversight and submitting audit tender reports and annual reports. There will also likely be additional costs remunerating audit committee members for their additional responsibilities and personal risk.

Three-quarters of investors believe this proposal will ensure audit committees act effectively as an independent body

Companies, however, are more likely to think the reforms will not achieve this

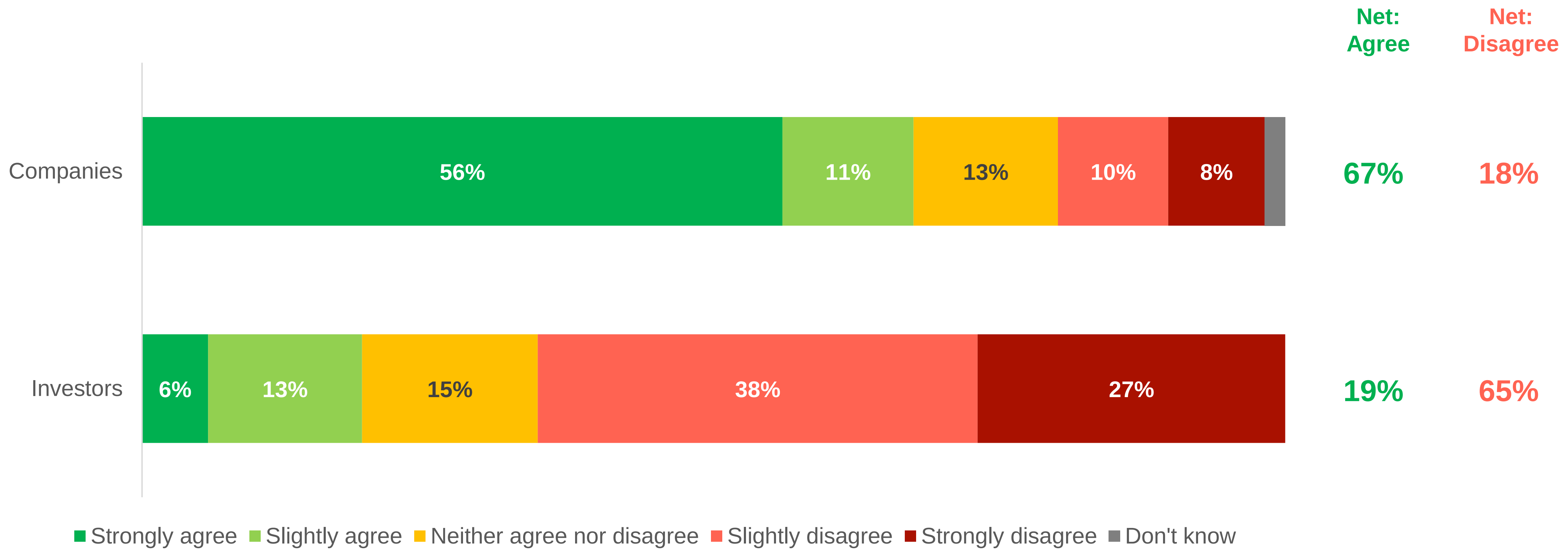
The Government proposes to give the regulator powers to set additional requirements as to the audit committee's role in the appointment and oversight of auditors to ensure the committee acts effectively as an independent body responsible for safeguarding the interests of shareholders and other users of accounts. To what extent do you believe this is achieved in the proposed reforms?



Base: all respondents (218); companies (166); investors (52)

While three-quarters of companies agree the proposals should only apply to FTSE350 companies, a similar proportion of investors disagree

To what extent, if at all, do you agree or disagree that the proposals should apply to FTSE 350 companies only, and not be extended to other PIEs?



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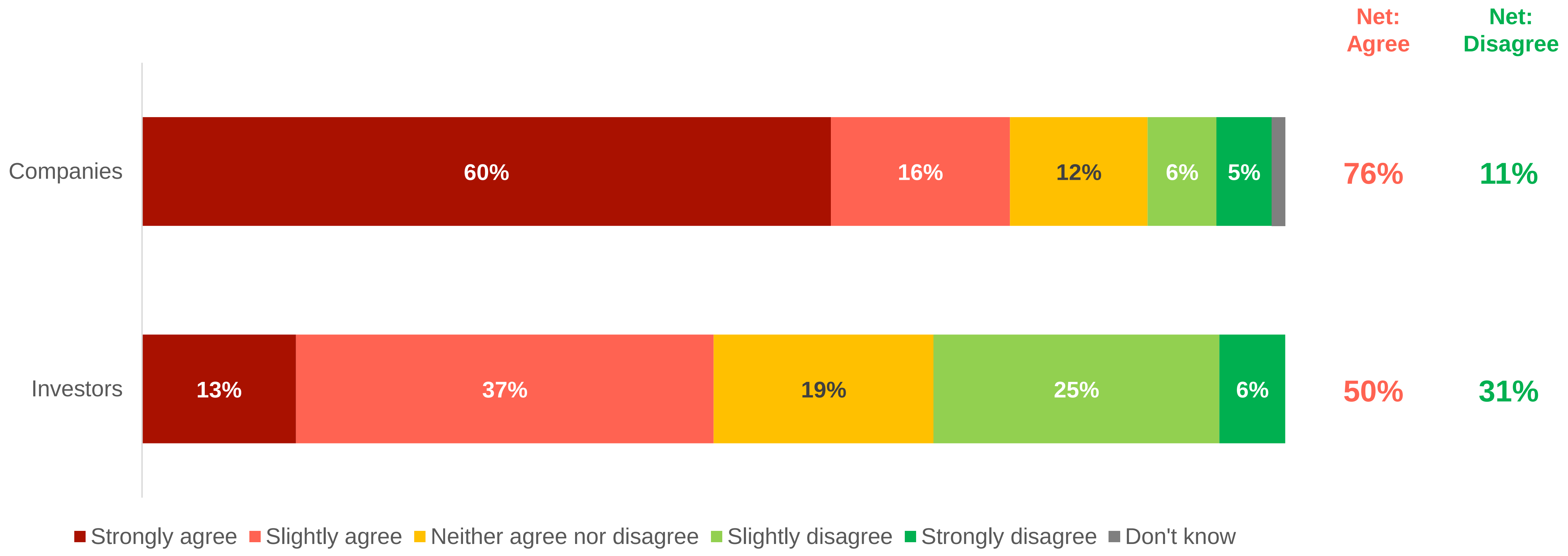
Three-quarters of companies agree that the regulator being able to place an observer on an audit committee could negatively impact audit committee discussions. Half of investors agree

To what extent, if at all, do you agree or disagree that the ability of the regulator to place an observer on an audit committee could disrupt the effective functioning of audit committee discussions?



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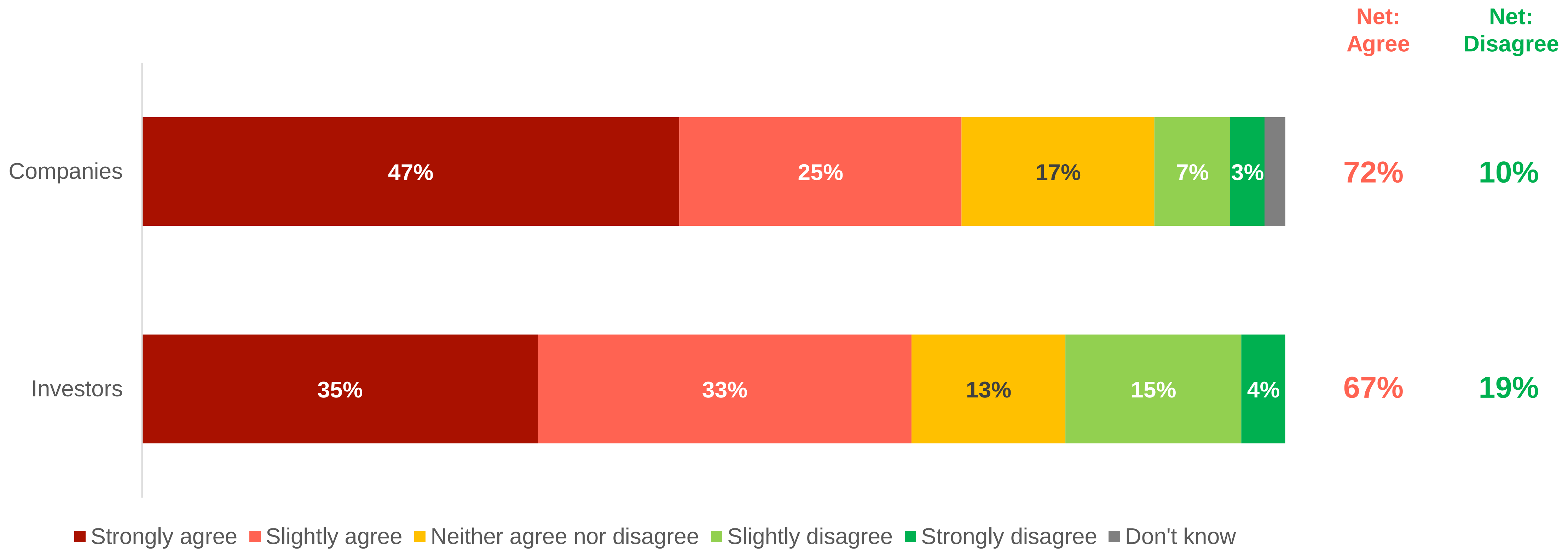
QUOTED COMPANIES ALLIANCE

Base: all respondents (218); companies (166); investors (52)

About seven in every ten of both companies and investors agree an audit committee's ability to seek an appropriate auditor could be impeded by the increased powers given to the regulator

To what extent, if at all, do you agree or disagree that giving the regulator the power to mandate requirements for the appointment and oversight of auditors, as well as monitoring and enforcing compliance, could impede an audit committee's ability to seek an auditor appropriate for an entity's specific circumstances?



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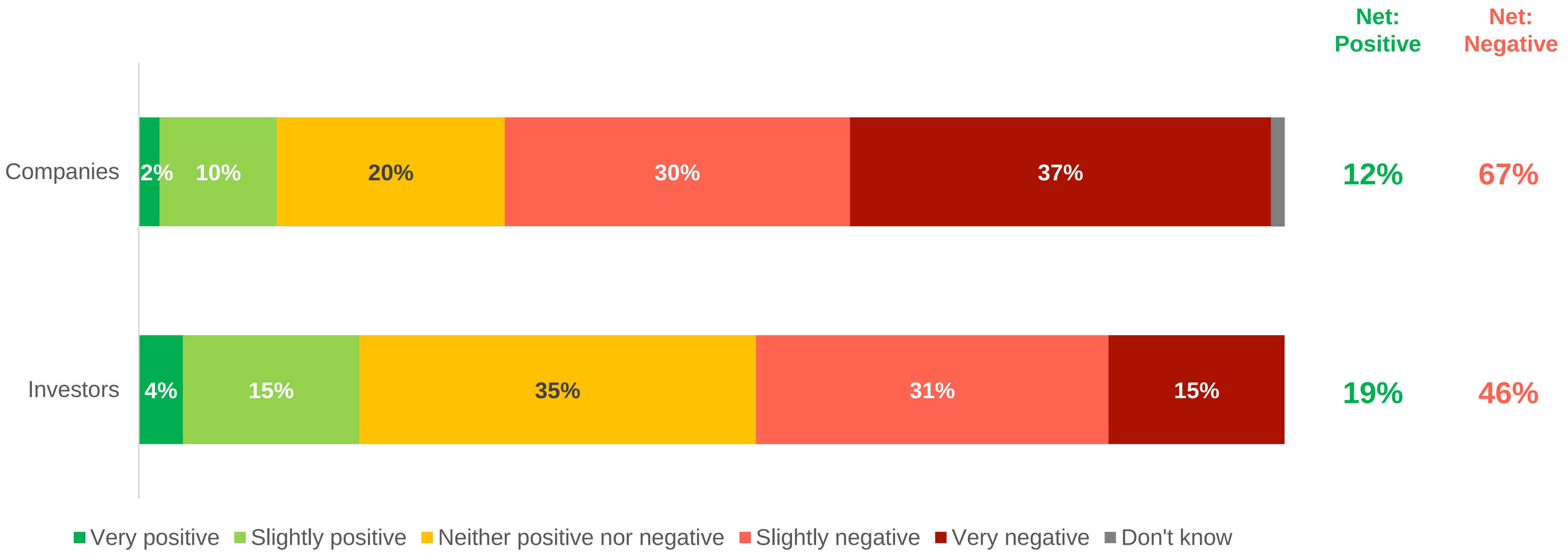
QUOTED COMPANIES ALLIANCE

Base: all respondents (218); companies (166); investors (52)

Both companies and investors are most likely to believe mandating prescriptive standards will have a negative effect on audit committee members

Just one in five investors, and a tenth of companies, believe mandating prescriptive standards will have a positive effect on audit committee members

What overall effect do you believe mandating prescriptive standards will have on audit committee members?



Base: all respondents (218); companies (166); investors (52)

Summary

- Having read through the proposals, three-fifths of companies believe that if the proposed reforms are implemented unchanged, there will be a negative impact on their growth.
- Nine-tenths of companies and four-fifths of investors believe the proposals have the potential to deter prospective individuals from becoming directors of publicly quoted companies.
- Both companies and investors believe the proposed reforms will lead to companies' boards spending more time on compliance matters. While companies estimate compliance currently takes around a third of board time, the new proposals would mean compliance taking around half of board time.
- Nine-tenths of respondents agree the proposed phased introduction of the requirements should be paused in order to conduct a comprehensive analysis of the impact of the reforms.
- The majority of respondents, both investors and companies, believe the current state of enforcement is effective in deterring malpractice.
- A third of companies believe the reforms will have a negative effect on the level of confidence that the UK is an attractive listing venue, although investors are more likely to believe there will be a positive effect.

Methodology

What?	20 minute online survey
Who?	166 x small-mid cap companies 52 x institutional investors
When?	10th May – 2nd June 2021

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Thank you for your attention!

The best panel, the best data, the best tools

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