

## Annex 5

### The role of specialists

In this Annex, we describe how the three groups of specialists referred to in paragraphs 3.20 - 3.24 of the submission help us to meet the audit requirements of large companies.

#### Controls Assurance / IT specialists

- 1 We have around 400 Controls Assurance specialists in our Risk Assurance business which forms part of the Assurance LoS. Large companies increasingly rely on IT systems with automated procedures to process a high volume of common transaction types. Ensuring that these systems have been properly evaluated to determine their robustness and sophistication is necessary before the audit team can reach an informed judgement on the reliability of system generated information and therefore the nature of evidence gathering procedures that is appropriate. With this understanding, an efficient audit plan can be deployed that avoids the need for ongoing validation of the many automated functions and reports.
- 2 Our Controls Assurance specialists understand IT systems and the specific risks created through their use. They are used extensively to test Business Automated Controls in Enterprise Resource Planning (ERP) environments such as SAP and Oracle, as well as in the financial services sector where complex systems are commonplace. ERP systems integrate internal and external management information across an entire organisation, including finance, manufacturing, sales and service, and customer relationship management information. They automate this activity with an integrated software application to facilitate the flow of information between all business functions. Auditing Oracle and SAP requires deep technical skills to understand fully the risks associated with the configuration and access to the system. [REDACTED]
- 3 Controls Assurance specialists are also valued by large companies to comment on the relative strengths and weaknesses of their IT systems, controls and management processes and to benchmark these systems against the best in class. This advice is invariably required as part of the overall audit service to large companies.
- 4 The team is also important to our drive to deliver a more efficient and cost effective audit service. The use of technology, centralisation of processes and increased reliance on controls has been a major contributor in delivering audit efficiency savings where we have been able to rely safely on central processes and technology.
- 5 We have been working with a number of large companies that have been transforming their operating systems, which has allowed us to “flex” our audit approach to rely on these new systems accordingly. This has involved providing proactive assurance as these companies implement complex systems or outsource / off-shore certain functions. Examples of large companies where our Controls Assurance specialists have been involved in such reviews include [REDACTED]. Our successful tender to [REDACTED] was in part due to our suggested approach to their new systems environment.
- 6 The demands made by large companies for Controls Assurance / IT specialists can be illustrated by the following client feedback:

- (a) [REDACTED]: *“With the change in the risk landscape, due to the migration to shared service centres and the majority of IT controls now in the hands of service providers, the scope of the controls-based work requires review.”; “I would value PwC’s perspective on how effectively we are managing the migration to the shared service centres, centralisation and the standardisation of systems” and “Through complementary assessments and solutions and via the utilisation of the best possible controls, the teams can maximise the value they bring to the business. Therefore part of PwC’s responsibility is to ensure that the teams work closely together, have an open dialogue and share reports and thinking. We are also keen for PwC to consider relying on Internal Audit if/when appropriate. The right balance needs to be struck to maintain independence yet utilise our internal testing, which may help to keep costs down.”<sup>1</sup>*
- (b) [REDACTED]: *“Real value will come from identifying the financial controls that could be systemised (e.g. automatic reconciliations) and therefore release the people operating them at the moment to do other things.”<sup>2</sup>*
- (c) [REDACTED]: *“PwC has got the right business understanding of the drivers for technology, systems, process, transformation, how the overall risk can be identified, what kind of activity of repositioning of our agenda with respect of the company strategy...PwC can provide the right support and the right skills, the right people”<sup>3</sup>*

## Accounting technical specialists

- 7 The growth of accounting standards in the UK and, more recently, globally with the development of International Financial Reporting Standards (IFRS), has required a greater awareness of these developments both by companies and by PwC. We have had an established Accounting Consulting Services (ACS) team for many years. The demands on the team, and its size, have increased considerably since the introduction of IFRS for UK listed companies.
- 8 The team in the UK now comprises of 42 highly experienced partners and senior staff. The senior accounting technical partner is supported by a further five partners, six directors and 30 senior managers and managers. This is not a purely technical environment. One key objective for the team is to share their knowledge and experience of firms with the wider audit practice. [REDACTED]
- 9 In addition, the UK ACS team links closely with the network’s central ACS team, drawn from firms across the network, [REDACTED], and again is supported by a multinational team of experienced senior managers and managers. The central team monitors developments in IFRS and, under the PwC network’s Chief Accountant, coordinates communications with the work of other PwC network ACS teams. The aim is to ensure that all parts of the PwC network have access to high quality specialist analysis and that IFRS is applied consistently. We are aware that the other large firms have similar structures, but from our experience this is not replicated in the mid-tier firms.

10 [REDACTED]

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<sup>1</sup> See Exhibit 23: [REDACTED].  
<sup>2</sup> See Exhibit 146: [REDACTED].  
<sup>3</sup> See Exhibit 14: [REDACTED].

- 11 The work performed by the ACS team directly supports the delivery of the audit service and also furthers the development of financial reporting. We note below a number, but not all, of the areas where the department provides its accounting expertise:
- (a) Interpretation and application of particular accounting standards, such as IFRS 2 “Share-based Payment” and IFRS 7 “Financial instruments: Disclosures” which are detailed technical standards, and also certain detailed UK GAAP standards such as FRS 17 “Retirement Benefits”. They advise on how issues should be disclosed in the financial statements, particularly on complex matters where significant judgement is involved.
  - (b) Technical reviews of a listed client’s financial statements, prior to issue, and also reviews of the financial statements of companies listing on the public market. In addition all FTSE 100 clients have an allocated ACS partner or director and manager to provide support to the engagement team throughout the year.
  - (c) Preparation of comment letters that respond to exposure drafts issued by the accounting standard setters (both international (IFRS) and UK GAAP). This includes coordinating the views of the audit practice, evaluation of areas of uncertainty and practical implementation of the standards and also considering areas for improvement and clarification.
  - (d) Development of accounting training courses for audit practice staff and developing the PwC Technical Update Seminars and Accounting Development Seminars for clients and non-clients. The team also produces a range of publications, including the PwC Manual of Accounting.
- 12 PwC has a desire to lead in the development of corporate reporting. One example of our UK efforts in this respect is our Building Public Trust Awards programme. Now in its ninth year, the awards programme reflects our view that both private and public sector reporting should encourage organisations to give better, not just more, information; improve the link between what is being reported and strategy; make sure narrative statements are backed by sound data; and set historic performance in context, especially when it is about future ambition. We used the 2010 Building Public Trust Awards event to launch an initiative to work with our clients on a voluntary basis to improve the level of disclosure in the audit committee’s report to shareholders of the debate that takes place between auditors and their clients.
- 13 That the largest firms have the ability and expertise in this area has been widely recognised:
- (a) Chartered Institute of Management Accountant’s response to the House of Lords Economic Affairs Committee call for evidence: *“International financial reporting standards (IFRS) are recognised as being complex. Proponents of IFRS cite the growing complexity in basic business transactions but nevertheless a significant amount of technical expertise is required by the audit firms to adequately advise their clients. The*

*Big Four firms not only have more people in their technical departments but these staff are exposed to similar issues in the dealings with other multinationals.”<sup>4</sup>*

- (b) The Oxera report: *“One FTSE 350 company that currently uses a mid-tier auditor commented that, while being happy overall, it found that its auditor is sometimes stretched when it comes to assessing the implications of new standards - the firm frequently has to resort to the texts published by the Big Four firms on these standards”.*<sup>5</sup>

## Other practice specialists

14 Supplying effective audit services to large companies requires us to draw on the expertise of a wide range of specialists from across the firm, including tax, treasury, valuations, actuarial, insolvency and economists. These specialists provide non-audit services directly to non-audit clients, but importantly assist the audit team in providing high quality audits where technical and complex issues affecting the financial statements arise. The specialists’ advice can be at either a relatively high level to offer a view as to the significance or otherwise of an issue, or in a considerable level of detail as required. By way of example:

- (a) tax specialists may consider judgements related to matters under negotiation with the tax authorities or where the application of tax law is uncertain;
- (b) treasury specialists may review valuation and hedge accounting matters related to complex financial instruments and derivatives;
- (c) valuations specialists may review a company’s assessments of whether assets might be impaired;
- (d) actuaries may typically review the reasonableness of the assumptions underpinning a company’s actuarial valuations and pensions accounting;
- (e) insolvency specialists may be involved in assisting the audit team to assess a company’s going concern statement, identifying where there have been, or are likely to be, breaches of banking covenants or liquidity issues; and
- (f) economists may review assumptions relating to aspects of the financial statements, such as inflation assumptions for pensions or the cost of capital used in impairment reviews.

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<sup>4</sup> See evidence of CIMA to the House of Lords Economic and Monetary Affairs Committee on 24 September 2010, page 76, Para 13 in response to question 1, Volume II of House of Lords Economic Affairs Committee 2nd Report – Auditors: Market Concentration and their role (published 30 March 2011)

<sup>5</sup> <http://www.publications.parliament.uk/pa/ld201011/ldselect/ldconaf/119/119ii.pdf>. Oxera report, page 24, paragraph 3.1.1.