

# Point of view

The UK Government's response to strengthen audit, corporate reporting and corporate governance for Investment Trusts

July 2022





# Introduction

On 31 May 2022, the UK Government published the long-awaited response to its proposals to strengthen UK's audit, corporate reporting and corporate governance systems. The proposed measures aim to enhance accountability across the business ecosystem, increase resilience and choice in the statutory audit market.

We published a 'Summary of the UK Government's response to the proposals on reforming audit and corporate governance,' comparing key measures in the response to the original consultation proposals. This is supplemented by EY's formative points of view on the key measures that are being taken forward.

These publications are a must-read for all Directors wanting to understand the full suite of changes impacting the market.

**Summary of the UK  
Government's response to the  
proposals on reforming audit and  
corporate governance**  
[Click here to learn more](#)

**Point of view**  
**The UK Government's response to  
strengthen audit, corporate  
reporting and corporate  
governance**  
[Click here to learn more](#)



# Purpose of this document

Whilst it is not possible to fully assess the balance of changes until we see the draft legislation and proposed amendments to the UK Corporate Governance Code (UK CG Code)<sup>1</sup> and Association of Investment Companies Code of Corporate Governance (AIC Code), we have prepared this document as an indicative guide for Investment Trust directors regarding areas that are likely to be most relevant to them, based on our current understanding. Our Investment Trust specific response to each measure does not repeat the full extent of details relating to each of the proposals, which can be found within the above publications.

Measure	Investment Trust within scope?
New entities in scope of the PIE definition	No
Directors' overall accountability	Yes
Supervision of corporate reporting	Yes
Internal controls systems	UK CG/AIC Code dependent
Fraud	No
Resilience Statement	No
Dividends and capital maintenance	No
Audit and Assurance Policy (AAP) and annual implementation report	No
Audit Committee (AC) oversight an engagement with shareholders	Yes (UK FTSE 350)
Competition, choice and resilience in the audit market	Yes (UK FTSE 350)
Malus and clawback	UK CG/AIC Code dependent with limited impact

*Note: whether an Investment Trust is within scope as defined above is based on a typical Investment Trust and all Investment Trusts should perform their own assessment.*

<sup>1</sup> The [FRC's July 2022 Position Paper](#) setting out how the Financial Reporting Council (FRC) will support the Government's reforms states that the FRC's intention is for the revised UK CG Code to apply to periods commencing on or after 1 January 2024. That will mean the FRC consults on a revised Code and supporting material from Q1 of 2023.



Key for icons used in the table below – consider the icon highlighted in yellow.

- ▶ Proposal dropped ☒
- ▶ Proposal taken forward ✓
- ▶ Proposal taken forward but significantly scaled back ⌚

*This key provides a non-Investment Trust perspective on whether the full suite of proposals included within the main consultation have been dropped, taken forward or scaled back. Our executive summary above and summary below explain whether the proposals impact an Investment Trust.*

CH	Measure	Investment Trust summary
1.6	New entities in scope of the PIE definition  ☒ ☑ 🔍	<p><b>Headline: New threshold and varying impacts on different categories of Public Interest Entities (PIEs).</b></p> <p>The definition of a PIE has been expanded to include entities with a turnover of £750m or more and 750+ employees. The new requirements for a Resilience Statement (RS), Audit and Assurance Policy (AAP), directors' statement on steps taken to prevent and detect material fraud and new measures on dividends and distributable reserves, will only apply to PIE companies that meet the size threshold.</p> <p>Investment Trusts are PIEs by virtue of listing and will continue to be PIEs. However, the vast majority of Investment Trusts will not exceed the 750 global employees' threshold and will therefore not be in scope for the new reporting requirements.</p>
5	Directors' overall accountability  ☒ ☑ 🔍	<p><b>Headline: New civil enforcement regime in relation to directors' statutory duties on audit and corporate reporting. No powers to prosecute offences.</b></p> <p>As Investment Trusts are PIEs by virtue of listing, the new civil enforcement regime in relation to directors' statutory duties on audit and corporate reporting will be applicable to Investment Trust directors.</p>
4	Supervision of corporate reporting  ☒ ☑ 🔍	<p><b>Headline: Entire annual report and accounts (ARA) in review scope of the Audit, Reporting and Governance Authority (ARGA) review. ARGA will have powers to direct changes.</b></p> <p>As Investment Trusts are PIEs by virtue of listing, ARGA will have power to cover the entire contents of their Annual Report and accounts. ARGA will also have statutory powers to direct changes to Annual Reports without having to seek a court order.</p>
2.1	Internal controls statement  ☒ ☑ 🔍	<p><b>Headline: Explicit statement by directors on controls effectiveness to be introduced through the UK CG Code (comply or explain). No mandatory assurance. The Audit and Assurance Policy (AAP) to state if external assurance is sought.</b></p> <p>Directors of Investment Trusts applying the UK CG Code will be required to make, on a comply or explain basis, an explicit statement on controls effectiveness. There will be no requirement to obtain external assurance over this statement and, as Investment Trusts will not have to publish an AAP, directors will not have to explain whether or not external assurance over the company's reporting on internal controls is sought.</p> <p>Whether Investment Trusts applying the AIC Code will be required to make an equivalent or similar statement will depend on, if and how, any new Provisions of the UK CG Code are transposed into the AIC Code.</p>

CH	Measure	Investment Trust summary
6.2	Fraud <input checked="" type="checkbox"/> <input checked="" type="checkbox"/> 	<p><b>Headline:</b> PIE directors to make a statement on steps they have taken to prevent and detect material fraud. No new obligations on the auditor.</p> <p>By virtue of having fewer than 750 global employees, the directors of Investment Trusts will not be required to make a statement on the steps taken to prevent and detect material fraud. Nonetheless, we would encourage directors to discuss fraud risk management considerations as part of the broader risk narrative in the annual report and accounts.</p>
3.1	Resilience Statement <input checked="" type="checkbox"/> <input checked="" type="checkbox"/> 	<p><b>Headline:</b> Risk, going concern and viability statement reporting expectations formalised and merged.</p> <p>By virtue of having fewer than 750 global employees, Investment Trusts will not be required to publish a Resilience Statement.</p> <p>The Government has a stated intention to identify deregulatory opportunities to simplify the existing framework for PIEs to alleviate some compliance burden on certain entities. As the Resilience Statement will, at a high level, combine the going concern and viability statements, there is an indication that the requirement for a viability statement will be removed from the UK CG Code. If this is the case, and a similar change is made to the AIC Code, Investment Trusts may be in a position where they are not required to produce either a resilience or a viability statement. If that is the case, we would encourage directors to understand investor expectations before discontinuing viability reporting.</p>
2.2	Dividends and capital maintenance <input checked="" type="checkbox"/> <input checked="" type="checkbox"/> 	<p><b>Headline:</b> Disclosure of distributable reserves is based on new guidance and is subject to audit, however no group estimate is required.</p> <p>By virtue of having fewer than 750 global employees, Investment Trusts will not be required, as a result of the new requirements, to disclose distributable reserves, include an explicit directors' statement confirming the legality of proposed dividends and any dividends paid in year or provide a narrative on board's long-term approach to the amount and timing of returns to shareholders under the requirements.</p> <p>Despite these requirements not impacting Investment Trusts directly, we view these as useful recommendations for the sector given stakeholders often place a high importance on an income objective Investment Trust's ability to pay a consistent and growing dividend. Enhanced narratives by directors on this topic would help to improve shareholders understanding of the Company's approach to dividends and may also help prevent illegal dividends from being paid. We highlight that Investment Trusts are already recommended to state which reserves are distributable (AIC SORP, Section 15).</p>

CH	Measure	Investment Trust summary
3.2	Audit and Assurance Policy (AAP) and annual implementation report  ☒ ☑ ⓘ	<p><b>Headline:</b> Summary of approach to assurance (internal and external) and to working with the auditor. No new mandatory assurance requirements being introduced.</p> <p>By virtue of having fewer than 750 global employees, Investment Trusts will not be required to publish an AAP or annual implementation report.</p> <p>In recent years, Investment Trusts have expanded the content of front half reporting to include new disclosures on topics such as ESG and in the future further climate related disclosures and publications are likely to increase as a result of FCA policy. Investment Trust Audit Committees should be considering the degree of confidence they have in the annual report content sourced from service providers and evaluating the appropriate level of assurance. In this context and considering that ARGA will have power to cover the entire contents of Annual Reports and Accounts, Investment Trust directors may wish to consider preparing an AAP, even if for internal purposes only.</p>
7.1	Audit committee (AC) oversight and engagement with shareholders  ☒ ☑ ⓘ	<p><b>Headline:</b> Minimum standards for ACs on appointment and oversight of auditors to be developed. Investor engagement to be driven via Stewardship Code.</p> <p>In respect of FTSE 350 Investment Trusts incorporated in the UK, ARGA will be given extended powers to set minimum standards relating to Audit Committees oversight and appointment of external auditors. In addition, all Investment Trusts will be impacted by intended legislation designed to improve the statements made by auditors ceasing to hold office.</p>
8	Competition, choice and resilience in the audit market - managed shared audits (MSA)  ☒ ☑ ⓘ	<p><b>Headline:</b> Mandatory Shared Audits (MSA) in and potential for market share caps.</p> <p>FTSE 350 Investment Trusts incorporated in the UK will be captured by the proposed new requirements to appoint a challenger firm as their sole group auditor or to appoint a challenger firm to conduct a meaningful proportion of the audit, with legal subsidiaries being the primary basis for the managed shared audit regime.</p> <p>The requirement for an MSA will be implemented over time and in a phased manner as audits fall to be tendered under existing tender cycles. An exemption framework will be developed, which, in limited circumstances will allow the regulator to grant exemptions or provide flexibility to companies seeking an alternative approach to identifying the 'meaningful portion' of their audit.</p> <p>It is presently unclear how an MSA regime would work in practice for single entity FTSE 350 Investment Trusts or whether these could apply for an exemption. The new requirements might therefore result in all FTSE 350 Investment Trusts having to appoint a challenger firm as their sole auditor in due course.</p>

CH	Measure	Investment Trust summary
5.2	Malus and clawback <input checked="" type="checkbox"/> <input checked="" type="checkbox"/> 	<p><b>Headline:</b> PIE auditor registration and oversight to move over to ARGA. Publication of individual AQRT reports will continue to require consent. The FRC needs to improve AQR process.</p> <p>The existing malus and clawback requirements impact premium listed companies via Provision 37 of the UK CG Code. As the majority of Investment Trusts have no employees and given the non-executive directors receive only a fixed amount of remuneration, Provisions 36 - 40 of the UK CG Code were not transposed into the current AIC Code on the basis they were not relevant. It is therefore unlikely that any future changes to the malus and clawback requirements will not have a significant impact on the sector given the limited nature of remuneration awards.</p> <p>We do highlight that the industry is increasingly discussing the need to consider clawback mechanisms in relation to performance fees paid to investment managers.</p>

# Contact us



**Maria Kepa**  
Director  
Governance and Public  
Policy  
[mkepa@uk.ey.com](mailto:mkepa@uk.ey.com)



**Caroline Mercer**  
Partner  
Asset Management  
Assurance  
[cmercer@uk.ey.com](mailto:cmercer@uk.ey.com)



**David Walker**  
Senior Manager  
Audit - Financial Services  
[dwalker3@uk.ey.com](mailto:dwalker3@uk.ey.com)

## EY | Building a better working world

EY exists to build a better working world, helping to create long-term value for clients, people and society and build trust in the capital markets.

Enabled by data and technology, diverse EY teams in over 150 countries provide trust through assurance and help clients grow, transform and operate.

Working across assurance, consulting, law, strategy, tax and transactions, EY teams ask better questions to find new answers for the complex issues facing our world today.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. Information about how EY collects and uses personal data, and a description of the rights individuals have under data protection legislation are available via [ey.com/privacy](http://ey.com/privacy). EY member firms do not practice law were prohibited by local laws. For more information about our organization, please visit [ey.com](http://ey.com).

Ernst & Young LLP

The UK firm Ernst & Young LLP is a limited liability partnership registered in England and Wales with registered number OC300001 and is a member firm of Ernst & Young Global Limited.

Ernst & Young LLP, 1 More London Place, London, SE1 2AF.

© 2022 Ernst & Young LLP. Published in the UK.  
All Rights Reserved.

EYSCORE 006312-22-UK

UKC-024126 (UK) 07/22. Creative UK.

ED None

Information in this publication is intended to provide only a general outline of the subjects covered. It should neither be regarded as comprehensive nor sufficient for making decisions, nor should it be used in place of professional advice. Ernst & Young LLP accepts no responsibility for any loss arising from any action taken or not taken by anyone using this material.

[ey.com/uk](http://ey.com/uk)