

Auditor independence – Audit committee chairs want changes to audit partner rotation

In March 2009 the Auditing Practices Board proposed a number of changes to their revised April 2008 Ethical Standards.

These cover a number of areas, including:

- appropriate period of time for rotation of audit engagement partners and engagement quality control reviewer of listed entity audits;
- remuneration and performance evaluation policies for key partners involved in audits;
- financial interests of new partners in the firm's audit clients;
- internal audit staff of the audit client working directly for the audit firm;
- provision of non-audit services to an audit client relating to

securitisation and restructuring services; and

- alignment to the IFAC Code of Ethics revisions

The key issue of concern has been the partner rotation period. The ICAEW undertook a survey of FTSE 350 audit committee chairs to ascertain their views, as major stakeholders in the independence process. Of the 121 audit committee chairs who responded to the survey, 78.5% supported extending the rotation period for audit engagement partners and engagement quality control reviewer of listed entity audits from the current 5 year requirement.

According to the postal survey, 54.5% of audit committee chairs would prefer a 7 year rotation period and 24% would prefer to retain the current period of 5 years but with additional flexibility to extend to 7 years if required. Only 21.5% wanted the status quo of 5 years retained.

Audit committee chairs who preferred a 7 year rotation period said that 5 years was too short given the time it took for engagement partners to understand their business and the issues involved. They also said that audit quality is enhanced by increasing the level of knowledge

of the audit engagement team and an understanding of the business issues.

Of those audit committee chairs who preferred a 5 year rotation period with the flexibility to extend, 79% said they believed this flexibility should be permissible for all listed companies. All said that any extension should be approved by the audit committee with 72% agreeing there should be disclosure in the report and accounts.

The results of this survey have been sent to the Auditing Practices Board. Further information on this and other ethics related matters is available at: www.icaew.com/ethics

Cash – everybody needs it but few take responsibility

Managing cash flow in uncertain times is something of a black art in that there isn't necessarily a right or wrong answer. However this is the time when the finance team can help other managers and directors to understand how to manage their working capital more effectively.

The UK economy has been in a state of turmoil for some time with mixed opinions as to when the turnaround will start. We can still expect to see some false dawns not to mention some green shoots that won't mature. The ICAEW UK Business Confidence Monitor has been showing the Confidence Index at a record low until the latest quarter and this lack of confidence and market uncertainty has forced businesses to slow down their stock and run down existing inventories. This change in the profile of working capital will need to change as businesses start to restock, but managing cash flow at this time will be critical.

So how can the finance team help educate the rest of the business? Too few small businesses accurately forecast their performance and therefore are surprised when cash crunches occur. Cash flow is something that affects all areas of a business but it all too often is seen as something that the finance function alone should manage.

Finance teams should work closely with operations and sales teams to dispel this myth.

Through collaborative management of a 12 month rolling integrated financial forecast all areas of the business can predict and understand the effects of certain purchasing and operational decisions. This model can help the sales team understand if their pricing policies are sufficient to cover the companies' costs and operations teams manage inventory.

These forecast models can either be detailed excel models or employ one of the many financial software tools in the market. Each has its merits but the principles and measures behind them are the same and these are what finance teams should be trying to teach their operational colleagues to help the whole business manage cash more effectively.

In addition the availability of finance in the market to help support businesses is starting to open up. For example, many banks have an appetite to lend on a secured basis e.g. through an invoice discounting facility. Most secure sources of finance however are united on one point: they will only lend to business managers who understand their own cash flows.

Cash flow and working capital management therefore are key to unlocking additional capital in the business as well as attracting new capital for growth and survival.

Debbie Clarke is a partner at CV Capital LLP, and Vice Chairman of the LSCA's London Business Board.

