Response to *Auditor Regulation – Discussion document on the implications of the EU and wider reforms*

INTRODUCTION:

This response is joint between the Group A and the members of the Association of Practising Accountants (we have appended a list of all of the firms which have ascribed to the response), namely the medium sized firms that are active in the mid-tier market, including SMEs[1]. For our complement of firms, there are several respects in which BIS' discussion paper represents an opportunity to improve the regulatory framework within which the profession operates, in a way that serves government objectives well, taking intelligent deregulatory steps and as a consequence liberating commerce to take advantage. To achieve that improvement, the implementation of the EU Directive and Regulation should be effected according to regulatory best practice: a recent report[2] which has Cabinet Office exposure and approval says that, *"The principle of proportionality should act as a 'gateway' test – regulation and regulatory practice which is not proportionate should be removed or improved as a matter of priority."*. In our firms' opinion, a judicious application of the principle of Proportionality in the course of implementation of the Directive and Regulation can bring about the benefits we point out in the balance of our response, and particularly in the Executive Summary that now follows.

We take the opportunity, especially given that it has been a long-held belief of our firms that meaningful regulatory intervention is the only way to correct the market distortion identified by the Competition & Markets Authority in the statutory audit market, to invite BIS to consider what additional means ought to be employed to correct the imbalance. We believe that addressing these issues is necessary in the public interest. In the absence of legislative compunction around Joint or Shared Audit, we believe that mandatory rotation and tendering mechanisms will fall short of objective. You will see that we therefore advocate the setting-up of an 'Implementation of Competition Objectives Working Group', to explore the potential of Joint or Shared Audit and other relevant issues.

EXECUTIVE SUMMARY:

Our principal submissions to BIS are as follows:

- The implementation of the Audit Directive and Regulation presents an obligation and an opportunity to have due regard to the regulatory principle of Proportionality. Considerations of proportionality must take full account of the likely future of audit and the shape of the audit profession. Proportionality in implementation of these new European measures will help the economy to deliver sustainable growth whereas the damage of heavy handed or inappropriate regulation in an ever-changing world economy will inhibit it.

  Proportionality of regulation is critical to growth, not only in the profession our firms are members of, but more importantly in broader commerce: we are part of a professional and business services industry whose performance is a key facilitator of

[1] In total, we have annual revenues of £1.1bn+, with 12,600 partners and staff in 230+ offices around the United Kingdom.

[2] *Benchmarking best practice for the regulators which govern the Professional & Business Services (PBS) sector*

growth in this broader sense. The regulator must operate in a way that complements our societal function, and commit to and lay emphasis on a liberalisation and deregulation of the professional accountancy market.

We strongly suggest that a joint **audit & accountancy working group**, comprising the profession and regulators should be set up, with the objective of converting commitment to the principle of Proportionality to a specific agenda, intended primarily to serve the end-user recipients of the professional services we provide. We should very much like to participate in such a group, which would go some way towards a concern on our part that we are very much under-represented at FRC level and indeed we understood it had been agreed by Group A and the FRC that such a joint group would be set up;

Unless sufficient attention is paid to Proportionality, regulation becomes a straightjacket and we commend BIS and the FRC's ready adherence to the recent Professional and Business Services Council's report we referred to earlier, which emphasises the importance of the principle.

We go on to make the following, additional, points:-

- The success of the regulator ought to be measured by the success of the profession it regulates; the regulator is not a proxy for the profession. Whereas we accept that enforcement is a part of regulation, the degree of current emphasis on it presents an existential threat to firms of our size, which do not present any systemic risk, our limited involvement in that tranche of activity renders us liable to regulatory sanction (both financial and bringing about real and lasting risk-to-reputation) that would not harm the largest firms but which would fundamentally endanger either our audit practising rights or our commercial viability.

  Reputation-risk and risk of financial penalty are simply disproportionate to our firms: they are not 'costs-of-business' and we are disproportionally affected by both. This has consequences for our capacity truly to compete with the largest firms, and for our ability to survive regulatory censure. Every stakeholder would surely accept, as the CMA does, that our involvement in the whole of the audit market is desirable, yet the conditions have not been laid by the FRC in which we may fairly be able to do that.

  We seek a balanced tone-at-the-top, where the sharing of professional knowledge and best practice become more clearly the major objectives of the regulator. BIS ought, in carrying out the implementation exercise in which it is currently engaged, to help bring about a change in tone, coupled with a commitment by the regulator to proportionate regulation;

- It is important that the governance of FRC be thoroughly reviewed to ensure that it is fit for purpose with the enhanced role it now has and this issue becomes even more imperative if it is to become the competent authority. There are potentially significant conflicts of interest within its broad remit, eg as standard-setter and enforcer of those standards. There is also a need for a review of the operation of the disciplinary scheme and the protection afforded to those subject to it, eg as to

maximum length of time before conclusion of proceedings and stage at which proceedings are disclosed.

That need is emphasised in our mind by the disclosure by Mr Haddrill at the said Open Meeting that it is intended that much more of the investigative and prosecutorial functions of the AADB are to be retained in-house by the executive, in an effort to address crippling costs. Moreover, a much more rigorous process for the appointment of board and key committee members is required.

- The current regulatory framework has many features that are both workable and that work in support of audit quality. We must be careful to retain the best features of the current regulatory framework, in which the role of the professional bodies is very important, and we must be especially careful that, in addressing issues relative to the audit of Public Interest Entities ('PIEs'), we do not adversely affect the operation of the rest of the regulatory framework, or cause changes made in relation to PIEs to trickle down, either at once or later, into the other parts of the audit market: the law of unintended consequences is always one to keep in mind.

- The definition of PIE is in itself an issue of great importance. Any suggestion that AIM-listed companies, and small charities (which similarly present no systemic risk), should be swept into it should be resisted: it is neither necessary nor desirable to bring the AIM market into the definition of PIE. The definition of PIE is… "*entities governed by the law of a Member State whose transferable securities are admitted to trading on a regulated market of any Member State within the meaning of point 14 of Article 4(1) of Directive 2004/39/EC*". AIM is not a regulated market for the purposes of that definition[3] and it follows that it would be permissible for the BIS and the FRC to adopt a more restricted definition of PIE, so as to exclude AIM (and ISDX).

  The benefits to end-user commerce would be substantial, and as we have pointed out in answer to Q4 below, the FRC itself believes that the additional assistance that audit firms could afford to the management of AIM-listed companies (but currently cannot by reason of the operation of ethical standards) would support the quality of financial reporting by those companies.

- Pursuant to the point we have just made, it will be necessary for the revision exercise by the FRC of its own Ethical Standards for Auditors to de-couple a part of the current definition of 'Listed entity' from the definition to be adopted of PIE. We advocate as unfettered a right on the part of end-users audited entities to Non-Audit Services as possible, on the grounds of support of the public policy principle of Growth. We therefore consider that the greatest restrictions on the provision of non-audit services should apply to fully-listed companies and not AIM-listed ones;

[3] AIM is owned and operated by the London Stock Exchange in its capacity as a Recognised Investment Exchange under Part XVIII of the UK's Financial Services & Markets Act 2000 (FSMA 2000), and although AIM falls within the definition of a Prescribed Market under FSMA 2000 and is subject to the UK market abuse regime, under the directives that form the EU's Financial Services Action Plan, it is not a Regulated Market.

- Although our firms advocate as many deregulatory/principle of proportionality-focused measures as possible, that should not be taken to mean that we do not wish to undertake the audits of PIEs: on the contrary, our firms are constituted and resourced so to do, they have the capability to do so, and the desire is present. We wish to expand our penetration of that sector of the market.

  We therefore strongly support the Executive Summary to the discussion-paper where, on p5, it says, "*The focus is on identifying legislative, and non-legislative, actions necessary to:…avoid excessive concentration in the audit market*". We believe that the BIS and FRC papers currently place far too little emphasis on promoting competition in the profession, especially with regard to the audits of PIEs.

  You will see from our responses that we advocate a number of regulatory interventions specifically intended to support this important public policy objective. We would therefore support engagement of the profession with the FRC (which we trust will have increased competition in its remit in future), and we also advocate the setting up of an 'Implementation of Competition Objectives Working Group', encompassing a wide range of stakeholders and regulators;

- The prospective 70% cap on the proportion of Non-Audit Services may bring about a means of increasing competition, by causing some of that work to be assigned away from the largest firms and thereby sensitising the boards and management of PIEs to the capabilities of firms other than those to which they have traditionally been predisposed. We suggest that the prohibition should attach not merely to the audit client but to affiliates of it or companies otherwise associated with it.

  Causing work simply to be recycled around the biggest firms would represent an opportunity lost, and we therefore invite BIS to have regard to how that consequence could be avoided. What we should be trying to achieve is large companies' growing awareness of the capabilities of competitor audit firms, through performance of Non-Audit Services; and

- We advocate caution so far as implementation of the Draft Statutory Instrument on the Accounting Regulations is concerned. We start from the premise that thresholds are a crude metric for measuring the thing that is important - audit risk.

  Raising the audit threshold would potentially increase the risk of fraud and material misstatements in financial statements and reduce the confidence of many business and other organisations when dealing with each other. It is virtually certain that an increased incidence of fraud and material misrepresentation of financial statements would follow the raising of the audit threshold: we have seen this sort of damaging result before and the empirical evidence lies in Insolvency Service records – we saw much media coverage in the 1990s about the failure of smaller companies and how dishonest behaviour caused ordinary creditors in turn to fail. The public disquiet was considerable.

The proposed raising of the audit exemption threshold would cause some £50bn of turnover to be taken out of audit examination, and the risk of damage to local economies and employers should not be understated.

Government should not be predisposed to a matching increase in the audit threshold and we have explained in our answer to Q41 why. Any further rise in the audit exemption threshold will, of itself, impair the professional learning environment and cause an irrational contraction in the numbers of Responsible Individuals the profession can train.

It must be appreciated that the critical skills that statutory audit practice instils in young auditors – professional scepticism, the appreciation of risk and relationship to going concern issues, attendance at stocktakes, dealing with management and interrogating it on material issues, understanding whole-business concepts, and adding value to the statutory process, are invaluable lessons that are learned not only through participation in PIE and major company auditing – arguably, they are *better* learned in firms where the audit chain-of-command is shorter. The raising of the audit threshold will inevitably bring about a loss of opportunity to train auditors, because it will take (according to figures supplied by BIS itself, we understand) some 7,000 companies out of the statutory audit obligation.

Audits currently being undertaken are societally important engagements: end-users need access to a well-trained audit firm population, given that entities of these kinds are of no interest to the largest firms. We cite as an example academy schools: Department for Education policy is heavily predicated on the need for academies' overall governance to be underpinned by statutory audit. Academies often appoint firms of our number for this purpose and the Department itself strongly encourages firms to develop a specialism that it depends on but which would be of no interest at all to the largest firms.

It is axiomatic that, if smaller firms' capacity to train auditors is constricted by the lack of opportunity that will present if the exemption threshold is lifted, then their capacity to service specialised-area clients will be constricted too.

EXECUTIVE SUMMARY CONCLUSIONS:

BIS has broader responsibilities than the FRC does: its interest is in protecting the Professional & Business Services part of the Growth Strategy, of which a vibrant and successful accountancy profession is but one part. Our overall message to BIS, and will be to FRC, is that (i) the key measurement of the success of any regulator ought to be the success of the profession it regulates (ie one that is competitive and broad based, vibrant and innovative), and that the regulator is not a surrogate for the whole profession, (ii) that our representations are intended to help bring to fruition the major policy-objectives that BIS has set for itself[4], and to ensure that the regulatory model for the profession is fit for the purpose of fulfilling those objectives; and (iii) that the UK adopts the new European Directive and

[4] Strengthen standards in PIE audit; improve confidence in auditors' independence; deal with market concentration; and make audit reporting more informative; and "*It is important that audit is a sustainable business, with adequate capacity and a diversity of suppliers meeting a variety of preferences,…and a more open market for non-audit services could also be expected to result*.".

Regulation Audit as purposively from the point of view of fulfilling those same objectives as possible, using the 'Member State options' as intelligently as possible.

We also make clear that the implementation of the Regulation and Directive should promote their stated goals in a manner which avoids gold-plating. We now set out our answers to the list of questions posed by BIS.

ANSWERS TO DISCUSSION QUESTIONS:

Q1. In relation to the measures discussed in both this (Chapt 4) and the next chapter, we would welcome comments on the balance between legislative and non-legislative implementation of the requirements of the new Directive and Regulation.

We favour the retention of as much discretion and flexibility as possible, consistent with implementation of the measures we advocate below. It follows that we do not advocate a predominantly legislative approach, though we consider that if implementation of particular aspects of the Regulation and Directive is led, for example, by FRC rather than BIS, it should demonstrate an equal commitment to the principle of avoiding gold-plating of European legislation. Moreover, whilst we have done our best to predict the what the downstream consequences of any given measure will be, it is almost inevitable that adjustments to regulations will be needed and it may be better to retain as much as possible in professional standards (or in secondary, rather than primary, legislation) for that reason.

Q2. In relation to all the Member State options in the Directive and the Regulation, we would welcome comments to inform our thinking on whether and how these should be taken up. Though many are discussed in this document and in specific questions, all the options in the Directive and Regulation are considered in the options tables that are being made available separately.

Having examined the options in the tables, we would be against the adoption of any that would tend to cause the United Kingdom to 'super-comply' in areas of Member State discretion. In addition, to ensure as much consistency across the EU as possible in the way the Regulation and Directive are implemented, we would encourage regard to be had to the way in which options are being exercised in other Member States.

In relation first of all to the Regulation, we cite para 2 (allowing a Member State to prohibit the provision of Non-Audit Services beyond those prescribed in the 'black list') of Article 5 of the Regulation, and para 4, sub-para 2 (placing additional restrictions on the provision of NAS otherwise allowed) of the same Article. Paragraph 3 of Article 5 allows a Member State to apply a *de minimis* exemption in relation to certain NAS[5] but we are not told what the exemption-threshold is.

Insofar as para 7 of Article 16 (entitlement of Member State to prescribe circumstances in which more than one audit firm should be appointed to a PIE) is concerned, we reiterate our view that, unless government takes as seriously as any other public policy objective the need for *proper, meaningful* regulatory intervention, particularly where systemic risk is greatest, then it will have done nothing to support the competition imperative of the CMA or fulfil the FRC's revised terms of reference, or properly address that level of systemic risk.

[5] "…in relation to preparation of tax forms, identification of public subsidies and tax incentives, support regarding tax inspections by tax authorities, calculation of direct and indirect tax and deferred tax, provision of tax advice, and valuation services by the statutory auditor".

In relation to Article 17 (mandatory auditor rotation), if government and regulator fail to acknowledge and address the risk that mandatory auditor rotation will merely cause a merry-go-round and interchange of PIE audits among the biggest firms and involve the smaller ones in crippling expense, firms of the latter size will be placed at a gross competitive disadvantage and subsequent disincentive to be active in the PIE market *at all*. It is important that consideration be properly given as to how firms in addition to the largest four can in total gain a reasonable share of the listed company audit market. This is necessary both for competitive and regulatory purposes as if one of the largest four firms were to leave the market it would be hard to see how regulatory capture could be avoided.

In para 4 of Article 24 (possible delegation of disciplinary sanctions to other bodies), we look forward to having sight of the consultation that BIS has in mind before answering definitively.

In paragraph (d) of Article 28 Member State has option to publish AQRT findings and conclusions in relation to specific inspections, we urge caution: the hitherto absence of a 'balanced scorecard' approach on the part of the FRC may cause the UK audit profession to be at a profound reputational disadvantage by comparison with the same profession in other Member States. We understand that the FRC has in mind a review of the current monitoring approach, content, and technique. We support the need for that review and look forward to contributing to it.

Turning now to the Directive, Article 1, para 2(f) in the Definitions section allows decisions on the wider application of certain requirements to non-PIEs to be a matter for the FRC. There is no clarity by what is meant by this part of the Table, nor what direction of travel the FRC might want to take with it and we should like to be provided with the necessary specification of intention. We particularly urge consultation with the profession around the definition of "major audit" in Schedule 10 to the Companies Act, paragraph 13(10), which determines the AQR inspection remit.

In Article 1, para 16, the UK has the option to continue the ES PASE derogation from the principal Ethical Standards for Auditors, and may allow FRC to consider going further in limited respects for audits of certain small undertakings, beyond the limits to which ES PASE currently applies. We should be obliged for clarity from the FRC in relation to what it may have in mind in this respect. We request the same clarity so far as Article 1, para 18 is concerned, on the potential simplification of requirements for audits of certain small undertakings, and so far as para 19 of Article 1 (the keeping of records by audit firms of minor infractions of the Directive), are concerned.

In relation to para 25 of Article 1 (potential disclosure of personal data in disciplinary decisions), it is unclear to us what BIS and the FRC have in mind and we seek clarification before commenting.

In relation to Article 1, para 26 (the principles of public oversight) and Article 32(4b) sub-paragraph 1 (extent of delegation of function), it will be seen from the balance of our responses that great care should be taken over which bodies should be assigned which obligations, and that the final architecture decided on should reflect an incorporation of adequate checks and balances. Our preference would be for legislation to delegate specific responsibilities directly to professional bodies by law to carry out certain tasks subject to FRC oversight.

Q3. In relation to the measures discussed in both this and the next chapter, what issues do you think arise that have not been considered as part of the discussion? If there are any, how do you think these should be addressed?

We have covered these in answer to other questions but essentially, we believe that there is an opportunity to redesign the whole accountancy regulation framework in a way that assists with government growth objectives and promotes a competitive, innovative and vibrant audit profession serving the needs of shareholders and wider society.

Q4. In relation to the measures discussed in both this and the next chapter, we would welcome comments on any burdens applied to small and micro sized companies and audit firms in particular by the proposed implementation, which you consider are disproportionate to the wider benefits?

Many of our answers address proportionality concerns in the round, so let us set out clearly at this stage, in answer to this question, that an opportunity presents for government to free up the SME sector (not just 'small' and 'micro' entities, as defined in the Regulation, but those that BIS would define as medium-sized and above), and the profession that services its needs most directly. Our principal representation is that it is not technical auditing standards that ought to change but *ethical* ones.

Most dedicated audit firms subscribe to the view that audit methodology, planning and execution are suitable and appropriate for all audited entities, irrespective of size, but a major distinguishing feature between PIEs and virtually everything else is the degree to which their internal financial reporting systems are properly set up and capable of preparing and presenting reliable financial statements.[6] Those companies may need external support that they, in our experience and according to research our firms have carried out, would often like to rely on their auditors to provide certain non-audit services but cannot, given the current prohibitions in relation to 'Listed' entities in the Ethical Standards for Auditors as currently drafted.

In support of our conclusion, we cite the FRC's project on quality of financial reporting for AIM and smaller listed companies, from which it falls to be inferred that, were the auditor to be allowed to provide reasonable assistance to AIM companies with regard to the preparation of their the accounts, it would significantly improve the quality in many instances.

We therefore draw a distinction between technical professional auditing standards and ethical ones for these purposes: whereas we see no need for changes in auditing standards, conversely the case for derogations from the ethical standards as they apply to Listed entities is cogently made out, in our view.

Our suggestion, therefore, is that when, as they must, the references in the ESAs to 'Listed' are substituted by 'PIE', the opportunity is taken to adopt a Member State option: the definition of PIE could be drawn so as to exclude public companies which are registered on the AIM[7]. The consequence would be significantly and purposively deregulatory.

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[6] As an FRC thematic on the quality of financial reporting in the AIM sector concludes, there is substantial empirical evidence of difficulty.

[7] Given that Article 1(2)(f) of the Directive defines a PIE as an entity that "…issues transferable securities that are admitted to trading on a regulated market in the EU", and AIM is not a regulated market *per* the definition, there is scope for the change we suggest to be adopted.

Purposive regulation does not imply a dumbing down of standards but provision ought to be made for a relaxation from those ethical standards that would otherwise apply to the audit of PIEs. The ownership of many public companies is quite narrow, much more so than the largest ones, so that the range of stakeholder is similarly narrow; they do not present a systemic or existential threat to the UK capital markets; and such external directly-interested stakeholders as they have (institutional investors, PE houses, etc) may, we believe, welcome additional auditor input in the preparation and preparation of their financial statements. Our suggested changes would support Audit Quality.

To apply the new provisions on PIE tendering and auditor-rotation to listed non-PIEs would be completely disproportionate and we therefore counsel against any potential for 'drift' of PIE provisions over time into AIM and below.

Q5. Do you agree that the Government should not expand the definition of a PIE beyond the EU minimum requirement – that is listed companies, banks, building societies and insurers? Please provide further information in support of your answer?

We have already suggested (see answer to Q4 above) that the definition of PIE ought not to attach to a significant number of public companies and for much the same reason, we are strongly of the view that the entitlement of a Member State under Article 1(2)(f) to designate any entity, because of its business, size, or the number of its employees, should be exercised only exceptionally, and that the entitlement should circumscribed by a set of carefully thought-through public interest identification-criteria. The presumption should be against classification as a PIE if the entity concerned is not caught by the main part of the definition.

Q6. What issues, if any, do you consider arise from the application of the provisions of the Regulation to audits of PIEs as defined in the Directive? How do you consider these should be addressed?

Our previous comments refer.

Q7. What issues, if any, do you consider arise from the need to broaden the application of the implementation of the 2006 Directive as amended to include:

- other entities whose securities are admitted to trading on a regulated market;
- electronic money institutions;
- payment institutions;
- MiFiD investment firms;
- Undertakings for Collective Investment in Transferable Securities (UCITS); and,
- Alternative Investment Funds (AIFs).

How do you consider these should be addressed?

Though entities of these kinds do not constitute a significant part of our market-sector overall, we have several member-firms which are significantly active in one or more of the areas highlighted in the Question (MiFiD investment firms, for example) and we do not believe, even given that the entities concerned are all involved in the provision of financial services of one kind or another, there is a compelling case for treating them all, irrespective of size, as PIEs.

We are mindful that there is so much - and such onerous - financial services regulation already at play that it is hard to see justification for adding more: simply because they are engaged in financial services is not a sufficient rationale for adding more if the entities themselves present little or no systemic risk.

Q8. What do you think are likely to be the familiarisation costs to auditors of PIEs arising from all the changes affecting them. In particular,
(a) how many person hours likely to be involved in an individual statutory auditor and their team understanding and preparing for the changes? This is a matter for individual firms to assess and so we do not respond as a group.
(b) what are the costs to audit firms of updating internal management systems to reflect the changes? This is a matter for individual firms to assess so we do not respond as a group. (c) How this is likely to vary by size of audit firm?
Given a significant element of fixed costs in such changes, time and direct costs are likely to be proportionally greater on average for firms other than the four largest. We add too that, whereas some of the larger mid-tier firms are already used to being regulated by the AQR, including its whole firm procedures, smaller medium sized firms such as those represented by APA, are not: the additional regulatory burden will be significant. Frankly, the more onerous the changes, the greater the risk that our firms will simply not wish, or be able economically, to adapt to them and may instead decide to exit the market.

Q9. Do you agree the FRC should be the single competent authority with ultimate responsibility for the audit regulatory tasks and for oversight under the 2006 Directive as amended by the new Directive and under the Regulation?
Our current view is that we do not consider, on balance, that the FRC should be the single competent authority. We make three points about this. First, our concern in this respect is that the size and development of the FRC has not been matched by an exercise in understanding its governance and ensuring the *adequacy* of its governance. Whereas we accept the legal obligation of Member States (through Single Competent Authorities) around PIE audits, it must surely be accepted by government that effective checks and balances must be in place to guard against capricious action, to ensure that real and meaningful accountability are hard-wired into governance, and that there is an effective recourse to external appeal.

The FRC was set up under, and still subscribes to, the conviction that it is an *oversight* body. The direction of travel (and this seems to have happened before the question of it being the SCA came along) is that it has tended to take to itself a number of direct operations and activities, carrying them out rather than truly supervising them. This is a profound qualitative difference in function and we believe a review of governance is needed to ensure appropriate checks and balances are in place with regard to the new structure to ensure a fairness of approach and to avoid conflicts of interest and the perception of such conflicts.

We are fundamentally opposed to the creation of any system whereby the FRC, set up as an oversight body, acquires operational activity over virtually all of the activities it was set up to oversee. That seems to us to be wholly wrong, dangerous, and counter-intuitive to the sound public policy objectives it was originally set up to serve. We doubt, having had access to legal opinion obtained by the professional bodies, that it is necessary to designate one, single, competent authority, and we certainly do not think it is desirable to create one that has such an amalgam of roles in one set of hands. To do so would amount, in our respectful opinion, to a constitutional nonsense.

Our second point is that, although the discussion paper makes clear that the SCA may delegate some functions reserved to itself, to other bodies (presumable the RSBs), it is opaque whether conditionality attaching to the act of delegation would fetter or empower the delegated body. There is therefore a necessary debate, essentially around the principles of natural justice, to be had in this respect before we would be in a position to comment

definitively. If we fail to have regard to these principles now, then we are simply setting up a problem of fundamental nullity for later on. As discussed elsewhere in our response, we tend to the view that the FRC should not be the sole competent authority.

Thirdly, the professional bodies and their working parties have a long history of issuing guidance to members on technical and other subjects. While having no statutory authority, that guidance is seen by many, including the Courts, as an expression of best practice. Appointing FRC as the SCA would be likely to remove all authority from such publications.

Q10. What issues, if any, do you consider arise from the need to implement a new statutory framework for the setting of auditing standards and for audit inspections, investigations and discipline by the single competent authority to replace the current framework that requires the bodies' rules to provide for this? If there are any, how should they be addressed?

On matters of auditing standards, this is a matter principally for the RSBs to address but we reiterate the point we made under our answer to Q9, that there are potential 'abuse of power and privilege' issues which can arise from circumstances where so many sets of power reside within one set of hands. Moreover, the accountancy profession is exactly that – a profession and civic society needs its liberal professions, which have been supported and nurtured for more than a century and a half by a structure predicated on much more than mere representation of members' interests. The RPBs have been trusted cornerstones in an overall architecture that works for the benefit of the public interest; it needs to be supported, not uprooted.

Q11. What issues, if any, do you think might arise for the current investigation and disciplinary arrangements between the professional supervisory bodies and the FRC, that apply to accountants generally as opposed to only auditors, given the changes in relation to audit? If there are any, how should they be addressed?

The answer depends on what the government sees as the major function of the FRC. Whereas the Regulation and Directive deal only with statutory audit, the FRC's remit extends to the whole accountancy profession. The dichotomy, of course, is that all, or virtually all, of its disciplinary jurisprudence, as well as all of its monitoring activity, is consumed by audit practice.

The same is true of the public interest in the FRC itself. By custom and practice, many see it is now synonymous only with audit, and the fact that most practitioners are active in other areas means that qualified persons are subject, somewhat arbitrarily to two distinct sorts of disciplinary jurisdiction. There seems an inherent unfairness in this and it should be said too that the disincentives to become a Responsible Individual are now seriously out of balance with the incentives to bring good, young, auditors into the fold.

Moreover, it is anomalous that FDs of listed companies and other public interest entities who are professional accountants are subject to the FRC's disciplinary scheme whereas those holding the same position but who are not professionally qualified do not fall within it.

The AADB Scheme and the Auditor Regulatory Sanctions Procedure should be reviewed as a matter of urgency. Tone-at-the-top is everything and we see a strongly coercive/enforcement narrative at the top of the FRC, which suppresses the educational/collegiate sort of regulation that is seen in other professions. We believe that that enlightened regulation should have its emphasis (not an exclusive one, of course) on building practitioner competence, not adversarial, and very retrospective, disciplinary proceedings.

Q12. In relation to each of the tasks provided for in the Directive and Regulation, do you consider that responsibility should be allocated to the single competent authority, for it to delegate to the professional supervisory bodies as appropriate and to the extent permitted in the Directive and Regulation? Please provide further information in support of your answer.
We have made representations in relation to this under our answers to the previous questions, pointing up the dangers of vesting too much authority and discretion in the FRC, especially under its current governance structure.

Q13. For any tasks where responsibility is allocated to the single competent authority for it to delegate, what limitations, if any, do you consider would needed to ensure that authority only retained responsibilities or reclaimed delegated responsibilities in appropriate circumstances? What do you consider these circumstances should be?
We believe that the allocation of boundaries ought to be a function of mature debate between BIS, the FRC, the RSBs, and the wider profession. We should take the opportunity that presents, to build a more modern consensus around what proportionality looks like in this sector of commerce.

Q14. In relation to each of the tasks provided for in the Directive and Regulation, are there any tasks, or any aspects of those tasks, that you consider it is important should continue to be covered by provisions in legislation on the content of the rules of the supervisory bodies? Please provide further information in support of your answer.
We have already made a number of comments in these respects under our answer to Q2 on the Member State Options tables. Our view is that the supervisory bodies discharge an important role in the public interest and that that role should not be removed, diluted, or changed by operation of the discretion of the new Single Competent Authority. It is not, as we understand it, incompatible with the notion of SCA for there to be more than one such body, although we accept that certain of the functions carried out an SCA cannot reside other than with a supervisory body such as the FRC. The remainder may be assigned, directly by BIS, to the supervisory bodies. We do not believe that the act of assignment should be within the gift of the FRC and that it should be dealt with in the course of the broader implementation process the government is now embarked on, and enshrined in primary and secondary legislation.

Q15. Do you consider that both the registration of statutory auditors and their removal from the register should be covered by regulations under the Companies Act? If so, which body or bodies do you think should have statutory powers for the removal of statutory auditors from the register?
The answer to this needs some context: our major concern here is that there is, on any view, no realistic likelihood that audit practising rights could ever be taken away from any of the biggest firms (audit practising rights are, of course, granted to firms, not to individuals), whereas it would be perfectly feasible to do so in relation to firms the size of our own, and smaller. The likelihood of that nuclear deterrent falling on those less able to defend themselves is a profoundly important ‘equality of arms’ point that needs to be appreciated at this vital point in time. Removal is an extremely serious penalty and should only be exercised by or with the express leave of the government, which in our view creates a necessary level of guarantee under the principles of natural justice.

We make a similar point in relation to the licensing of audit firms, which is currently in the gift, under their exercise of powers originally granted under the Companies Act 1989, of the

supervisory bodies. The licensing function should continue to reside with those bodies, leaving oversight of the licensing regime to the FRC; to assign the right to the FRC to license audit firms is tantamount to ceding the oversight role – the more that the FRC adopts operational functions, the less it can fulfil its original establishment as an oversight body. We therefore support the suggestion, on page 19 of the discussion document, that the responsibility for approval of RIs and firms as eligible for appointment as statutory auditors should be given directly to the professional bodies (and the responsibility for removal in instances not involving AADB action as well).

It follows that (i) we expressly oppose the suggestion in the immediately preceding paragraph on page 19 that the FRC should take overall responsibility for approval, but delegate it to the professional bodies, and that (ii) there should be no *"additional approval requirements for auditors conducting certain audits such as major audits"* (penultimate paragraph on the same page). A power such as this could very easily be applied in a capricious executive manner which resulted in prejudice to the mid-tier and smaller audit firms.

Q16. Do you consider that, for consistency with a framework of ultimate responsibility, single competent authority approval should be required for the rules of the supervisory bodies?

Again, this is a question of who should be the ultimate arbiter of the suitability and adequacy of RSBs' rules – if it is being suggested that it ought to be the SCA, then we think that is fundamentally objectionable, for the reasons we expressed in our answer to the previous question. The rules of the professional bodies should be pre-approved and given a statutory foundation at the point of implementation in UK law of the Regulation and Directive. Future amendments should reside in the joint discretion of government, the SCA, and the professional bodies.

Q17. What do you consider are the costs and benefits in monetary terms and in terms of the effectiveness of audit regulation of the proposals in this chapter and of your preferred approach to implementation of these provisions?

We cannot conceive that the new regime will result in cost-savings, and rather depressingly, we can only anticipate increased costs, which the end-user audited entities will have to bear. As discussed earlier, we also believe they bear disproportionately on non-Big 4 firms. We cite with approval p17 of the discussion-paper, "*We consider that the following are the main considerations in identifying the best way of meeting the overall direction of the EU measures….minimising the costs of audit regulation.".*

Q18. Do you agree that the provisions of Article 4 of the Regulation on the cap on non-audit services should be included in amendments to the FRC's ethical standards for auditors? Please provide information to support your answer.

We believe the cap does have a role in encouraging competition, and believe that the ESAs are the best place to accommodate the 70% cap.

Q19. What issues, if any, do you consider arise from the application of the provisions on the cap on non-audit services? If there are any, how do you consider these should be addressed?

The devil will inevitably be in the detail, and it remains to be seen how firms can make intelligible sense out of averaging out the levels of NAS they have been providing to an audit client in any consecutive period of three years. The cap does seem to be more appropriate and workable for ethical standards than legislation.

We agree that the issuing of comfort letters in connection with prospectuses issued by the audited entity should be excluded from the 70% cap but believe that the exclusion should extend to other sorts of comfort letter where the audited entity is mounting a takeover bid or attempting to defend against an unwanted bid.

Q20. Do you agree that the Member State options in Article 4, to set more stringent requirements on the cap and on the auditor's independence where their total fee income from a PIE exceeds 15% of their total fee income overall, should be capable of being applied by the FRC in its ethical standards for auditors? Please provide information to support your answer.

We doubt that any of the biggest firm could conceivably ever be affected by this provision but given that there are similar provisions already in the ESAs already, there seems to us no compelling reason for dealing with the same territory in a different way or place, or in a more stringent way.

Q21. Do you agree that the FRC should have the ability to exempt an audit firm from the 70% cap for up to two financial years on an exceptional basis and on application by the firm?

Given that the proposed cap has been exceeded in recent times on far more than an exceptional basis, care would need to be taken, if this proposal did go ahead, to ensure that exception was only allowed on a genuinely exceptional basis.

Q22. Do you agree that the subject matter of Article 5 of the Regulation on the blacklist of non-audit services, including the possibility of setting more stringent requirements, should be included in amendments to the FRC's ethical standards for auditors? Please provide information to support your answer.

We restate our representation that PIE should exclude AIM (and ISDX and GXG-listed companies) and confirm that the means of enforcing the cap should reside in the ESAs.

Q23. What issues, if any, do you consider arise from the application of the provisions on the blacklist of non-audit services? If there are any, how do you consider these should be addressed?

It would be helpful to have a roundtable discussion on the direct and indirect consequences of the blacklist, pointing up in an annotated version of the ESAs where the main changes will occur, and how the fact that the implementation-date will be retarded affects anything. It should be borne in mind that the purpose of the blacklist is to identify aspects of the provision of Non-Audit Services which affect the auditor's independence, and to cause those services to be provided by another firm. It should not be forgotten that the operation of the black list offers an opportunity to fulfil another of the objectives of EU implementation – the stimulation of the audit market through sensitising end-users to the capabilities of other firms, even if initially through the redistribution of NAS.

Q24. Do you agree that implementation of the revised requirements on ensuring and documenting auditor independence in the 2006 Directive should be implemented primarily via the ethical standards, with amendments to the existing legislation as necessary only to:

(a) underpin the standards? And,

(b) introduce simplifications for audits of small non-PIEs?

Please provide further information to support your answer.

Yes, we do. The IESBA Code, on which the ESAs (and the RSBs' Codes of Ethics) are based, is well understood and embedded in UK firms and their international networks and

was referred to at length during the *Barnier* discussions that preceded the new Regulation and Directive.

Q25. Do you agree that the existing framework on disclosure by PIEs in notes to their accounts of the audit and non-audit fees they paid their auditor should be adapted, to ensure public disclosure of the information the auditor is required to provide to the competent authority under Article 14 of the Regulation? Please provide information to support your answer.
As this seems the corollary of the obligation on audited entities, yes, we do.

Q26. For our impact assessment on the changes we would welcome any estimates that could be provided on:
(a) the percentage of non-audit services that are likely no longer to be provided by auditors due to their inclusion on the blacklist? Whilst we cannot give a precise calculation in this area, we expect the black list to result in the prohibition of a high percentage of non-audit services. However, it should be noted that as commented on in our response to question 4, Ethical Standards for Auditors currently prohibit many of the services included on the black list.
(b) the additional costs associated with reallocating some of the non-audit services that would otherwise have been provided by the same statutory auditor? The additional costs would include those incurred in relation to the initial appointment of the non-audit service provider, both by the PIE and by the provider as well as those incurred by the provider in then obtaining a more detailed understanding of the entity which would require input from management. Subsequently, we expect the difference in costs incurred were a firm distinct from the auditor providing the non-audit service compared to a scenario where the audit firm provides the non-audit service to be minimal given that, if the auditor had previously provided the non-audit service, a team separate from the audit team would in all likelihood have carried out the non-audit work as a safeguard to the threat otherwise posed to auditor independence.
(c) the extent to which these additional costs vary by the size of PIEs? We consider the size of the PIE to be less relevant than the complexity of the PIE – the more complex the PIE, the greater the investment required by the non-audit service provider in Year 1 of the engagement.
(d) the person hours likely to be involved in a non-audit team at an audit firm understanding and preparing for the changes given that they will not be able to provide certain non-audit services to the firm's audit clients? We anticipate that the initial costs in responding to these changes would be incurred by the auditor in considering their independence rather than by the non-audit team. However, as noted above, the services prohibited by the EU Audit Regulation do not present a substantial change from those prohibited by Ethical Standard 5.
We believe that developing a robust impact assessment will require substantial discussions and analysis but believe the questions posed are of rather too general a nature. We strongly advocate a separate implementation discussion in these respects, lest the law of unintended consequences brings about the contraction of competition that we have warned of elsewhere in our response.

Q27. Audit Committees must submit a recommendation to the board for the appointment of an auditor. However, under Article 16(1) sub-paragraph (2) of the Regulation, this does not apply where the Member State has provided an alternative system for the appointment of the auditor. The current alternative systems set out in the Companies Act 2006 are where:
• the directors appoint the auditor before the company's first accounts meeting;

• the directors appoint the auditor to fill a casual vacancy in the office of auditor; and where,
• the Secretary of State appoints the auditor because a public company failed to do so.
Do you consider that all of these alternative systems for the appointment of an auditor should continue to operate in the UK as they do at present? Are there any other systems that should also be provided for on the grounds that a competitive tender process is not appropriate? Please provide further information to support your answer.
We believe the current arrangements are broadly satisfactory.

Q28. Where the PIE is exempted from having an audit committee (eg because it is an unlisted bank), there is no provision as to which body should fulfil the audit committee's role. Do you agree that in this situation the directors should determine the recommendations that should be put to shareholders of the audited entity? Please provide information in support of your answer.
We would expect unlisted PIEs generally to have audit committees as a matter of good practice. If there is not one, allowing a vote by the directors seems the best, if second-best, alternative.

Q29. The Government does not intend to take up the option to provide for an extension of the maximum duration of the engagement beyond 10 years where a joint auditor is engaged. Do you agree that the replacement of a single auditor with two joint auditors, one of whom was the original auditor, should be made on the basis of a retender? Please provide further information in support of your answer.
We have made submissions previously, both as the mid-tier and in some cases as individual firms. We said then, and we maintain, that if government is meaningful about addressing the Competition issue, then the only means of doing so is direct and substantial regulatory intervention. Joint Audit and Shared Audit would accomplish the aim but were means drowned out by the power of others' lobbying. We believe further consideration of both is essential and we can see no reason why the extension to twenty four years as provided by the Regulation is not being adopted. Failure to adopt this Member State option constitutes gold-plating as audit committees are allowed to appoint joint auditors. The CMA outcomes were, in the sense of stimulating audit firm competition, insipid, and given that the FRC was encouraged by CMA to take on a specific remit around the stimulation of that competition, it has a clear opportunity to do so.

Q30. We are considering whether provision should be made so that, where a PIE has stated in its annual report it will appoint an auditor based on a tender process before the expiry of the maximum duration of 10 years, it should still be able to take advantage of an extension of the maximum duration beyond ten years, following that tender. Do you agree?
Yes.

Q31. We are seeking views on the proposal that for companies that are PIEs the company's plans on retendering should be part of a new element of the annual report setting out key matters for the audit committee on the appointment of auditors. Do you agree that the report should include:
a) when the current auditor took up the audit engagement at that company? (Yes / No)
b) when the audit engagement was last retendered? (Yes / No)
c) the start of the next accounting year in relation to which the company expects that the auditor appointment will be based on a tender? (Yes / No)
d) the directors' reasons for considering that the proposed year is in the best interests of the company's members? (Yes / No)

Do you consider that any other information should be included in addition the above? Please provide further information to support your answer.
The annual report should make clear how the company is getting to know a sufficiently wide range of firms. It should also disclose in the year ahead of the next tender how it proposes to involve all firms eligible to bid for the tender.

Q32. We are considering whether, where the statement under point (c) above is included in the company's annual report, and the incumbent auditor is reappointed on the basis of the planned tender process before the expiry of the 10 year maximum duration (eg at 7 years), the next tender process should be expected to take effect:
(a) after the same period has expired again (ie year 14 in this example);
(b) after a further 10 years has expired (ie year 17 in this example); or,
(c) after the same period has expired again, though with the potential to extend it by the full 10 years via further notice from the audit committee in the annual report (ie in this example at year 14 though this could be extended to year 17)?
Which option would you prefer? Please provide further information in support of your answer.
In line with our approach of generally seeking to avoid gold-plating of the Regulation, we believe option (b) is the most appropriate. There should not be any expectation that, because a company decided to tender before 10 years for whatever reason, it should then be locked into always having to operate to a shorter tendering cycle.

Q33. What issues, if any do you consider arise from the UK's obligation to apply effective, proportionate and dissuasive sanctions for failure to comply with the UK's implementation of the framework on mandatory rotation and retendering? If there are any such issues, how do should they be addressed?
It will, of course, be necessary to attribute blame to the party causing the obstruction but we believe, given that the perpetrator may be the audited entity, that sanctions would be better enshrined in statute or subordinate legislation.

Q34. For our impact assessment on the changes we would welcome any estimates that could be provided on:
(a) resources that are likely to be deployed by PIEs to tender audit appointments?
(b) resources that are deployed by auditors to tender for audit work?
(c) additional familiarisation costs that arise for both auditors and the audit client when a new auditor takes up an audit engagement?
(d) the extent to which this varies by the size of the PIE?
We note that the Competition Commission ingathered sufficient information on audit tender costs which we trust is immediately available.

Q35. What issues, if any, do you consider arise from the inclusion in legislation on audit reporting of a requirement for the auditor to include a statement in the audit report where there is a material uncertainty relating to events or conditions that may cast significant doubt about the entity's ability to continue as a going concern? How do you consider these should be addressed?
We do not believe that the inclusion in legislation of a requirement for the auditor to include a statement in the audit report where there is a material uncertainty concerning going concern will have a significant impact, given that this requirement is already included in ISA 570: if there is a material uncertainty over the appropriateness of the going concern basis, an

'emphasis of matter' paragraph may be inserted. We question why this requirement needs to be included in legislation at all given that it is already included in the ISAs.

If codified in legislation, we presume there would be penalties laid down in law, rather than by the regulator, for failure to comply with this provision.

Q36. Do you agree that the provisions of Article 10 of the Regulation on the audit report should be included in amendments to the FRC's International Standards for Auditing (UK and Ireland)? Please provide information to support your answer. We consider that the changes to audit report requirements should be included in the ISAs which should form a definitive set of standards.

In line with our views on gold-plating, the provisions of Article 10 should only be required *per se* in the audit reports of PIEs.

Q37. What issues, if any, do you consider arise from the application of the provisions of the Regulation on the audit report? If there are any, how do you consider they should be addressed? The principal provision relates to the reporting of significant risks and the auditor's response to them, a requirement which has already been implemented in the UK by the FRC which has stipulated that the audit report must include 'key audit matters'. Hence we do not expect to see any further significant impact as a result of Article 10.

There clearly may be different audit reports for PIEs than for other entities, if our preferred approach is adopted. Much in this area is already included in the audit report for companies on the London Stock Exchange, as the FRC amended ISA 700, and this measure extends it more widely to all PIEs. Inclusion in auditing standards is sensible.

Q38. Do you agree that the provisions in Article 11 of the Regulation on the additional report to the audit committee should be included in amendments to the FRC's International Standards for Auditing (UK and Ireland)? Please provide information to support your answer.

Yes. The issues covered in Article 11 are intended for reporting to the audit committee and not necessarily to the shareholders.

Q39. What issues, if any, do you consider arise from the application of the provisions of Article 11 of the Regulation on the additional report to the audit committee? If there are any how should they be addressed?

It will naturally be important for the audit committee to consider what information they wish to include from the Article 11 report in their audit committee report to shareholders.

However, we do not agree with BIS' assumption that extra work will not be created: extra time will be needed to prepare the report itself, even though it will not add much to the scope of the audit work – there will be extra requirements for communication with those charged with governance.

Further, we do not support the use of the term 'verify' ('*describe the methodology used including which categories of the balance sheet have been directly verified*'), as it could lead to misleading impressions of the purpose of an audit and expectations of what it can achieve. We assume that the phrase we have highlighted means what has been substantively tested but this should be clarified in relevant amendments to auditing standards.

We point it out in our answer to Question 40 but we expect increased costs to occur, and to relate largely to Article 11, Provision 2(g).

Q40. For our impact assessment on the changes, we should particularly welcome data on:
(a) additional resources are likely to be needed by the auditor to produce the additional report for the audit committee?
(b) the additional annual cost of the audit committee considering the additional report?
(c) how these costs vary by size of PIE?
The amount of resources will naturally vary according to the size of and complexity of the client and issues arising in the course of execution of the audit. We will be happy to participate in a more detailed exercise to assess potential costs, if helpful: an anticipatory discussion of this kind will be important to conduct.

The requirements of the audit committee report are largely consistent with our current reporting to audit committees and so, except in the case of the detailed requirements of Article 11, Provision 2(g), we do not expect that significant further additional time costs will be incurred.

Q41. Do you consider that the small companies audit exemption thresholds should:
(a) remain aligned with those for the small companies accounting regime, so that the number of audit exempt small companies will increase in line with the increase in the small companies accounting thresholds;
(b) remain unchanged so that the turnover and balance sheet thresholds are considerably lower than the thresholds for access to the small companies accounting regime; or,
(c) be amended in some other way (please set this out)?
Please provide further information in support of your answer.
No. We have already commented on the damaging effect on auditor training-capacity, and we emphasise it: an essential part of the overall regulatory architecture around statutory audit is the learning environment in which we train young auditors, who need to have experience of all sizes of audited entity, otherwise the consequence will be a contraction in the capacity to train Responsible Individuals, which will in turn continue to fuel the FRC's fears around sustaining viable numbers of statutory auditors.

At a time when concern is already being expressed by regulators and other commentators that the practice of audit does not constitute the major part of many large firms, in terms of revenue, the consequence of a further lifting of the thresholds will be to contract the field of properly licensed and experienced practitioners, condensing the capacity to audit among only a very few firms, very much at the top end of the market. The visibility of impact will be muted as that will not matter to the largest firms but it means that smaller entities and those that are still obliged to have an audit (charities and academies, for example) will be denied access to a larger practising population, leading to further contraction in the availability of auditors.

We say too that an increased incidence of fraud and material misrepresentation of financial statements would be another unwelcome consequence of raising the threshold: we have seen this sort of damaging result before and the empirical evidence lies in Insolvency Service records.

On a conservative estimate, the proposed raising of the audit exemption threshold would cause some £50bn of turnover to be taken out of audit examination[8], leading to a profound loss of public confidence. We believe that the accounting and audit thresholds should be the same, but maintained at current levels. Changes made in the name of deregulation will not bring about welcome consequences in the medium and long terms.

We strongly advocate to BIS that specific, detailed, further discussion needs to be undertaken in order to assess adequately the regulatory impact of the raising of the threshold and any failure to do so would, in our view, amount to a breach of proper process. The representations we are making are supported by the professional bodies, we should add.

Though it remains to be seen, the further discussion we advocate may conclude that the thresholds for small company accounting and auditing exemptions should remain aligned only if they are all set at the lowest possible limit for small company thresholds rather than the highest. At £10m turnover, a company is simply too big to be exempt from any form of financial scrutiny – a change of threshold of this level of materiality is not deregulatory; it is an abrogation. If a Member of the House of Commons is faced in his or her local constituency with the failure of an employer-company exempted from audit on the basis that its turnover was less than £10m and a three-figure loss of jobs results, voluble public concern is not difficult to foresee.

There are simply too many risks attendant on change without further study and we need to make sure that we do not cause mistakes of history to be repeated.

Moreover, we are at a moment of major wholesale change in UK financial reporting, which may suggest that the audit threshold decision should usefully be delayed until we have seen how businesses have coped with dealing with FRS 102.

Q42. What issues, if any, do you consider arise from the measures considered in this chapter? If there are any, how do you consider these should be addressed?
We have alluded to these in other answers.

Q43. For the purpose of our impact assessment, we would welcome any information you can provide on the expected costs and benefits of the measures considered in this chapter, particularly any estimates of costs or benefits that you consider it would be possible to quantify?
In addition we remind you that the general questions asked at the start of chapter 4 also apply to the measures discussed in this chapter.
Please see above comments in relation to Articles 10 and 11. As discussed, we believe a proper assessment will require detailed studies and we will be happy to contribute to such an exercise.

Q44. Do you agree that the implementation of EU requirements on technical standards should be primarily through changes to the FRC's ISAs (UK and Ireland)?
Yes.

Q45. For the purpose of our impact assessment on the changes we would welcome any estimate you could provide of the percentage of PIE audits for which the quality control

[8] Derived from the Professional & Business Services Council 'think-tank' of BIS.

review will now have to be undertaken by an individual auditor from outside the appointed audit firm (where there is a lack of detachment from the audit or knowledge of the client sector) where this was not previously required?
We estimate the number would be negligible, though we would suggest that specific outreach ought to be made (whether by BIS, the FRC, or the supervisory bodies) to small and very small firms which audit PIEs.

Q46. What issues do you consider arise from the implementation of EU adopted ISAs in the UK that UK representatives should raise with the European Commission?
We are not aware of significant issues: the additional provisions are largely similar to those already imposed in the UK – our principal concern is ensuring that they are applied in a proportionate manner and hence our key argument is that we believe that AIM listed entities should not be included in the definition of PIE.

The ability to supplement ISAs should be retained (see below, for our answer to Question 47).

Q47. Do you agree that following any adoption of ISAs by the European Commission, the FRC should have the discretion to:
(a) apply standards where the Commission has not adopted an ISA covering the same subject-matter; (Yes / No) We believe that the FRC should retain this discretion to enable it to respond to local issues and maintain investor confidence but it should be applied very sparingly.
(b) impose procedures or requirements in addition to adopted ISAs if these national procedures or requirements are necessary to give effect to national legal requirements or to add to the quality of financial statements? (Yes / No) As above
Please provide further information in support of your answer.
We believe that (a) and (b) are best considered on a case-by-case basis but the option of developing standards or additional requirements in such circumstances should be retained, and we advocate separate consultation on the generality of the ground covered by this Question.

Q48. What issues, if any, do you consider arise from the implementation of the new requirements on audit committees via amendments to the existing DTR 7.1 in the FCA Handbook (for companies with securities admitted to trading on a regulated market)?
Essentially, this is a matter for Audit Committee Chairs to comment on.

Q49. What issues, if any, would you consider arise from the implementation via provisions in PRA rules of the new requirements on audit committees for those banks, building societies and insurers that are not required to have an audit committee under DTR 7.1?
Many such institutions already have audit committees as a reflection of good governance and so we do not envisage significant issues arising. We again make the same point as we did in answer to Q7, however, that not all PRA-regulated entities ought logically to be considered to by PIEs, given the lack of systemic risk many of them tend to present.

Q50. For our impact assessment on the changes, we would welcome data on:
(a) the numbers of non-listed PIEs that currently do not have an audit committee?
(b) the cost of recruiting members to be part of an audit committee?
(c) the annual cost of attendance of a member?
(d) the auditor's fees for attending audit committee meetings?

(e) how these costs vary by size of PIE?
Separate consultation is again recommended, though we add that our firms may make individual responses, as the Question bears on their particular circumstances.

Q51. Do you consider that the single competent authority with responsibility for regulation of audit should be designated to receive the information required to be provided to supervisors of PIEs when it is provided to:
(a) the PRA for banks, building societies and insurers?
(b) the FCA for other PIEs? or
(c) both?
We would have thought that it is desirable for statutory gateways of this kind to exist, for public interest protection reasons and because it may cause multiple-regulatory exposure to be lessened, though we caution against the potential for over-burdensome consequences: if it means that the FRC would require to be informed of any qualified audit report on a PIE. A similar proposal was mooted by the FRC some years ago, and rejected on the grounds that it amounted to an over-burdensome obligation and might unnecessarily trigger a Corporate Reporting Review.

Q52. For the purpose of our impact assessment on these changes we should be grateful for any estimates you can provide of:
(a) the costs of the auditor providing this information to supervisors of PIEs?
(b) the frequency with which the PRA is provided with this information for banks building societies and insurers under existing requirements?
(c) the frequency with which the FCA is provided with this information for other PIEs in practice already?
We would not expect significant incremental costs in addition to those already incurred in dealing with the PRA and FCA.

Q53. Do you agree that we should enable the single competent authority to exercise the choices of aptitude test and/or adaptation period for the approval in the UK of individual statutory auditors from other Member States? Please provide further information in support of your answer.
No. Given that the SCA will be wholly comprised of non-auditors, there needs to be another mechanism for adjudication on important matters like the capabilities of auditors qualified in other Member States.

The approval of auditors from other member states could perfectly properly be carried out by the supervisory bodies.

Q54. Were the single competent authority to have this role, what do you consider would be the implications for the operational provision (currently by the professional supervisory bodies) of:
(a) aptitude tests; and
(b) adaptation periods (if these were to be provided for)?
How would this be affected by the CEAOB progressing discussions "with a view to achieving a convergence of the requirements of the adaptation period and the aptitude test" across the EU?
These are matters that need meaningful qualitative judgements to be made and as we said in answer to Q53, it is inappropriate for them to reside within the SCA.

The Group A and APA firms