



LONDON SOCIETY
OF CHARTERED
ACCOUNTANTS

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Regulation and Ethics Review Panel

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Dear Paul,

AUDITOR REGULATION: DISCUSSION DOCUMENT ON THE IMPLICATIONS OF THE EU AND WIDER REFORMS

I am writing as Chairman of the Regulation and Ethics Review Panel (RERP) of the London Society of Chartered Accountants (LSCA). The LSCA is by far the largest of the 22 district societies affiliated to the Institute of Chartered Accountants in England and Wales (ICAEW). It has a membership of 34,000, representing nearly one quarter of all ICAEW members, and also provides services to other ICAEW members who live or work in London. London members, like those of the Institute as a whole, comprise a mixture of those working in all sizes of practice and those working in businesses, both large and small, or otherwise not in practice. They also include many of the ablest and most senior Chartered Accountants, together with a wide range of specialists.

RERP welcomes the opportunity to comment briefly on this discussion document. We have seen a draft of the ICAEW representation and endorse this in full. The focus of RERP is on the ethical and regulatory aspects of proposals as they affect auditors rather than on more technical issues and this is reflected in our comments below.

GENERAL COMMENTS

We agree with the ICAEW view, as expressed in the Overview section of its response, that it is important not to lose sight of why the European Commission initiated the review of auditor regulation in the first place as a response to perceived shortcomings in the audit process in the wake of the 2008 financial crisis.

Its main purpose was to address the audit of banks and the largest and most complex Public Interest Entities (PIEs) that could pose systemic risks to financial stability and market confidence. This focus should be reflected in the Government's approach to implementation of the Regulation and the Directive.

We support the view that there should not be change for the sake of change nor unwarranted extension of regulation beyond the minimum required by the Regulation and the Directive.

We would expect the Government to adhere to its stated principles of regulation and to seek to avoid going beyond the minimum requirements of the measures being transposed into the UK regulatory framework.

We would also challenge the view that the FRC should be the only competent authority and are concerned that the role of the professional bodies as regulators be maintained to the maximum extent possible.

Particular regard should be had to not placing unwarranted additional burdens on small enterprises and their auditors.

SPECIFIC COMMENTS

We will not attempt to deal in detail with each of the 54 questions raised in the consultation. A few key observations about the main changes are, however, set out below for your consideration.

Question 1: We support the ICAEW view that using legislation, to achieve delegation of significant responsibilities, should not undermine the commitment to minimum regulation.

Question 2: We agree with the ICAEW view that MSOs should be taken up where they maintain something that is fit for purpose, assist practicality and flexibility of implementation, and minimise the cost burden on business.

Question 3: There is a need for a review of the suitability of the existing governance arrangements for the FRC, not least in the light of possible increases in its powers, in order to ensure that there is appropriate accountability in place.

Question 4: We would not wish to see any erosion of the exemptions available to smaller business and their auditors beyond the unavoidable minimum.

Question 5: We agree that the Government should not expand the definition of a PIE beyond the EU minimum requirement.

Question 9: We do not agree that the FRC should be the single competent authority and share the concern of the Institute that the proposals in the discussion document place the FRC in an unhealthily powerful position without appropriate checks and balances, pose considerable regulatory risk and weaken the role of the accountancy profession itself in leading and developing the delivery of audit at best quality standards. We support the view that the current arrangements work well and do not need to be changed significantly, other than to meet the requirements of the Regulation in respect of PIE audits.

Question 12: See response to question 9. We share the ICAEW view that there is neither a requirement nor a need for a single competent authority in respect of non-PIE audits.

Question 13: We support the ICAEW view that the setting up of the present RSBs as competent authorities for relevant regulatory purposes would enshrine necessary safeguards for ensuring responsibilities are not unnecessarily transferred to the ultimate competent authority.

Question 15: We do not believe there is a need to change the present arrangements for the registration and removal of statutory auditors whereby the RSBs deal with these matters.

Question 16: We do not consider that there needs to be a specific requirement that the single competent authority approve the rules of RSBs. The FRC already has an oversight role that encompasses this.

Question 17: We share the concern that costs will increase substantially for medium-sized firms with a small number of PIE audits because of the additional inspection arrangements.

Question 18: We agree that provisions on the cap on non-audit services are best dealt with as amendments to the FRC's ethical standards for auditors.

Question 19: We share the ICAEW view that the whole basis for a cap on non-audit services is unjustified and would support minimum implementation.

Question 20: We agree that the MSO to set more stringent requirements, where the total fee income from a PIE exceeds 15% of total fee income for the firm, should be capable of being applied by the FRC in its ethical standards for auditors. We question, however, the need to do so.

Question 21: We 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.

Question 22: See response to question 20.

Question 24: We 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 the minimum of legislative changes. The introduction of simplifications for small non-PIE audits should be encouraged by the use of MSOs covering a range of matters.

Question 25: We 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.

Question 27: We consider that all of the current alternative systems for the appointment of an auditor should continue to operate in the UK as they do at present but do not believe there is a need to provide for any additional systems.

Question 28: We agree that, where the PIE is exempted from having an audit committee, the directors should determine the recommendations that should be put to the shareholders of the audited entity.

Question 29: We note that the Government does not intend to take up the MSO to provide for an extension of the maximum duration of the engagement beyond 10 years where a joint auditor is engaged. The minimal use of joint audits in the UK market suggests that this is not likely to be a point of contention and we would not object to this stance being taken.

Question 30: We agree that provision should be made so that, where a PIE has stated in its annual report that 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 10 years, following that tender.

Question 31: We agree with the proposal that PIEs should include their plans on retendering in their annual report and have no objection to the proposed disclosures, even though they go beyond what is required in the Regulation and could be criticised on that ground.

Question 32: We agree with the ICAEW that the analysis seems overcomplicated. The basic premise of the Regulation that there should be tendering at least every 10 years and rotation at least every 20 years should be adhered to.

Question 33: We agree with the ICAEW view that there are likely to be few instances in practice of non-compliance with the mandatory rotation and retendering requirements. Any sanctions should be proportionate.

Question 36: We agree that the provisions of Article 10 of the Regulation should be included in amendments to the FRC's ISAs.

Question 41: We support in principle the continued alignment of the small companies audit exemption thresholds with those for the small companies accounting regime. The raising of the audit threshold is, however, a significant matter and we concur with the ICAEW view that it should be the subject of a separate consultation. We would, therefore, seek to defer any change in the audit threshold until such consultation has taken place.

Please do not hesitate to contact me, if you have any queries or wish to discuss any of these matters further.

Yours sincerely

Bruce Picking