BLACKROCK

19 March 2015

Paul Smith
Corporate Frameworks, Accountability and Governance
Department of Business, Innovation and Skills
1 Victoria Street
London,
SW1H 0ET

Sent electronically to: pauld.smith@bis.gsi.gov.uk

Re: Auditor Regulation - Discussion document on the implications of the EU and wider reforms

Dear Mr. Smith,

BlackRock is pleased to have the opportunity to respond to the Auditor Regulation - Discussion document on the implications of the EU and wider reforms.

BlackRock is a leading provider of asset management, risk management, and investment advisory services to institutional, intermediary, and individual clients worldwide. As of 31 December 2014, the assets BlackRock manages on behalf of its clients totalled £2.99 trillion across equity, fixed income, cash management, alternative investment and multi-investment and advisory strategies including the iShares® exchange traded funds.

BlackRock has a pan-European client base serviced from 22 offices across the continent. Public and private sector pension plans, insurance companies, third-party distributors and mutual funds, endowments, foundations, charities, corporations, official institutions, banks and individuals invest with BlackRock.

BlackRock represents the interests of its clients by acting in every case as their agent. It is from this perspective that we engage on all matters of public policy. BlackRock supports policy changes and regulatory reform globally where it increases transparency, protects investors, facilitates responsible growth of capital markets and, based on thorough cost-benefit analysis, preserves consumer choice.

We welcome the opportunity to address, and comment on, the issues raised by this consultation and we will continue to contribute to the thinking of the Department of Business, Innovation and Skills (BIS) on any specific issues that may assist in improving the implementation of the Auditor Regulation. As financial statements preparers and users, we have a considerable interest in the impact of this legislation, particularly with regard to our investment funds based in the United Kingdom and throughout Europe.

We have set out our comments to your questions in a separate response form. We have responded to the questions we consider relevant to ourselves as a corporate entity, and as an investor. Our overriding view is that any available option that restricts the audit committee's ability to determine the most qualified audit firm for specific services should be avoided.

Key points

Maintain the prohibited list of non-audit services rather than replace with a 'white list'

We do not support amending the prohibited list of non-audit services under Article 5.2 of the Regulation by replacing it with a 'white list' of permissible non-audit services. We believe there are other safeguards in place where an audit firm may be engaged for such services to mitigate threats to audit firm independence and to protect investor interests such as all non-audit services requiring approval from the audit committee (after having assessed the threats and safeguards to auditor independence).

The new UCITS and AIFMD depositary regime justifies the audit committee exemption

We support the audit committee exemption available for UCITS and AIFs in Article 39.3 (b) of the Directive as these funds are subject to a well-established regulatory regime and additional specific governance requirements such as the appointment of an independent depositary. In addition, we support the audit committee exemption in Article 39.3 (a) where the group audit committee is discharging the requirements that would be imposed on a Public Interest Entity's (PIE) own audit committee as this exemption avoids any duplication that would otherwise occur where a PIE would have to create an audit committee in addition to one that already exists at the group level.

No reduction to the 70% non-audit fee cap

We do not support any reduction to the 70% non-audit fee cap under Article 4.2 of the Regulation as we consider that there are existing safeguards regarding independence. We believe any reduction could result in the creation of 'pure audit firms' which we do not support. We have concerns that such firms may not be able to attract staff of suitable quality because of the lack of opportunity offered compared to multi-disciplinary firms, with a consequent adverse impact on audit quality. Accordingly, we believe that the cap of 70% under Article 4.2 should not be reduced.

70% non-audit fee cap effective date

We welcome BIS stating in this Discussion document that they consider the first calculation for the cap must be undertaken in respect of the accounting year beginning on or after 17 June 2019 (i.e. the 4th accounting year beginning after the application of the Regulation). This provides companies with sufficient time to change their non-audit service providers or auditors, if required, in an orderly and considered manner.

Potential extra-territorial application of the legislation

We have concerns that Article 5.4 in the Regulation implies that the PIE's audit committee (or the group audit committee acting on behalf of the PIE) would have to pre-approve all permissible non-audit services provided by the statutory auditor (including its member firms) even if they are to be provided to non-EU parent entities or non-EU controlled undertakings. We understand that the European Commission's Q&A on Implementation of the new statutory framework dated 3 September 2014 (the European Commission's September 2014 Q&A) in relation to an analogous question "*What if the audit client has subsidiaries which operate in different jurisdictions (EU and non-EU) which are required to*

apply different auditor rotation rules?" clarified that "The Regulation does not have any extraterritorial effects – it applies to PIEs that operate within the EU only. Thus, if a PIE incorporated in the EU has a subsidiary incorporated in a third country, there is no legal obligation upon this PIE to rotate its auditors in this third country, unless the law of the latter states so."[1] Applying this analogy would result in the PIE's audit committee having a duty to pre-approve non-audit services for controlled undertakings of the PIE and its parent within the EU, not those outside the EU. This is consistent with our interpretation of the legislation but we would welcome this being clarified by BIS.

10 year extension to audit tenure after a public tender

In order to mitigate the additional risk to a PIE resulting from auditor transition, and to allow the development of institutional knowledge, BlackRock supports the 10 year extension permitted by the Regulation where a public tender has been undertaken. Requiring rotation after 10 years reduces the competitiveness of the tender process and results in additional start-up time and costs for new auditors, which reduces the savings and investment returns for Europe's citizens and employers.

A service such as investor tax reporting should not be prohibited

Germany, the UK, Switzerland and Austria all require detailed per unit taxable income information to be provided to investors. If this is not done, the fund will not have tax status in that jurisdiction and the investors will pay excessive tax on their holding in the fund. This is a high volume activity, so to illustrate BlackRock provides well in excess of a million pieces of tax data per annum under these tax reporting regimes taken together.

Much of the calculation work is undertaken by fund administrators, but typically there is a very large process involvement by one of the Big 4 audit firms. Most fund managers choose to get a degree of independent tax compliance assurance over the figures, and further in Germany it is requirement of the tax regime that a licensed steuerberater (tax adviser) certifies the key tax disclosure figures. Owing to the highly operational, high volume nature of the process, moving between tax service providers requires lengthy planning.

We believe that services such as investor tax reporting should be permitted to be carried out by the audit firm or a member of its network. We are concerned that removing the possibility of using the fund auditor for this work will reduce choice and competition in this material, specialised tax services market to an unacceptable degree. Investor tax reporting has no direct or material impact on the financial statements of a PIE, nor does it involve any advice or element of discretion to the fund itself. Rather, the consumer of the service is the end investor, who uses the data to complete their tax return. Therefore, we would suggest that BIS clarify that investor tax reporting is not a prohibited service under this legislation with reference to Article 5.3 of the Regulation.

[1] The European Commission's Q&A is available here:
http://ec.europa.eu/internal_market/auditing/docs/reform/140903-questions-answers_en.pdf

Yours sincerely,

Colin McDonald
Director

Tom McGrath
Director

Department for Business Innovation & Skills

AUDIT REGULATION

Discussion document on the implications of the EU and wider reforms – Response Form

DECEMBER 2014

Regulation on the Specific Requirements Regarding Statutory Audit of Public Interest Entities and Directive amending Requirements on Statutory Audits of Annual Accounts and Consolidated Accounts

Discussion document response form

The Department may, in accordance with the Code of Practice on Access to Government Information, make available, on public request, individual responses.

The closing date for responses is 19 March 2015

Name: Colin McDonald/ Tom McGrath
Organisation (if applicable): BlackRock Investment Management (UK) Limited
Address: 12 Throgmorton Avenue, London EC2N 2DL

The form can be submitted by email or by letter to:
Paul Smith
Corporate Frameworks, Accountability and Governance
Department of Business, Innovation and Skills
1 Victoria Street
London,
SW1H 0ET

Tel: 020 7215 4164
Email: pauld.smith@bis.gsi.gov.uk

Please tick a box from the list below that best describes you as a respondent.

	Business representative organisation/trade body
	Non-government standard setting/regulatory body
	Charity or social enterprise
	Individual
√	Large business (over 250 staff)
	Legal representative
	Local Government
	Medium business (50 to 250 staff)
	Micro business (up to 9 staff)
	Small business (10 to 49 staff)
	Trade union or staff association
	Other (please describe)

Chapter 4

Q1. In relation to the measures discussed in both this 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.

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 the discussion 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.

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?

In order to mitigate the additional risk to a Public Interest Entity (PIE) resulting from auditor transition, and to allow the development of institutional knowledge, BlackRock supports the 10 year extension permitted by the Regulation where a public tender has been undertaken. Requiring rotation after 10 years reduces the competitiveness of the tender process and results in additional start-up time and costs for new auditors, which reduces the savings and investment returns for Europe's citizens and employers. We welcome BIS clarifying the tender/rotation timeline where an incumbent auditor of a PIE has been appointed as auditor for fewer than 11 consecutive financial years as at 17 June 2014 through publishing the additional supplementary information[1] which it states that:

"It is true that on 17 June 2016, some audit engagements under the third transitional provision will be of more than 10 years' duration, and up to 13 years' duration. This is because the transitional provision covers audit engagements for financial years that began on or after 17 June 2003. This will be the case for all audit engagements for which the first financial year began between that date and 16 June 2006.

For these audit engagements, we consider that the auditor of the accounts for the financial year beginning before 17 June 2016 is still able to complete the audit of those accounts. However at the start of the first financial year beginning after that date, the auditor could not be reappointed to audit the accounts for that year other than on the basis of a tender."

This clarification is helpful in removing uncertainty for companies falling into the 'less than eleven years' category where there had been some ambiguity around the financial periods affected.

[1] BIS, AUDITOR REGULATION – SUPPLEMENTARY INFORMATION, The implications of the EU and wider reforms, March 2015.

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?

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?

☒ Yes ☐ No ☐ Not sure ☐ Not applicable

We agree that the Government should not expand the definition of a PIE further and beyond the EU minimum requirement as we believe it would add unwarranted complexity and cost.

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?

We support the audit committee exemption available for UCITS and AIFs. These funds are subject to a well-established regulatory regime and additional specific governance requirements such as the appointment of an independent depositary with a duty to maintain ongoing oversight over the fund's assets. Accordingly we believe the incremental costs associated with requiring audit committees for these types of entities outweighs the benefits. Similarly, we support the exemption where the group audit committee is discharging the requirements that would be imposed on a PIE's own audit committee. This exemption avoids any duplication that would otherwise occur where a PIE would have to create an audit committee in addition to one that already exists at the group level.

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?

MiFiD investment firms, UCITS and AIFs (collective investment schemes) are regulated and governed under other legislation and regulation within the UK relating to requirements for an annual audit, appointment/dismissal of auditors, independence requirements and qualification/disqualification of auditors. We believe that simply broadening the application of the implementation of the 2006 Directive in Part 42 of the Companies Act to include these entities could potentially bring in competing legislation that these entities need to comply with. For example open-ended investment companies (OEICs), which can be either UCITS or AIFs, are not companies under the Companies Act as they are not trading entities, but rather corporate entities with their own facilitative legislation that has been drafted specifically with the needs of collective investment schemes in mind. In principle it would be preferable if consequential amendments are made directly to the Open-Ended Investment Companies Regulations for OEICs or to the Financial Services and Markets Act and FCA implementing rules for authorised unit trusts. We would recommend that BIS consult separately with HMT on how best to make amendments to the legislation and regulations which govern the operation of collective investment schemes.

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?

(b) what are the costs to audit firms of updating internal management systems to reflect the changes?

(c) How this is likely to vary by size of audit firm?

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?[2]

☒ Yes ☐ No ☐ Not sure ☐ Not applicable

We agree that for the reasons of efficiency and co-ordination the FRC should be the single competent authority provided it has sufficient funding and resource to discharge its responsibility to implement the revised Auditor Directive and Regulation along with its other responsibilities.

[2] In answering this question, it may help in particular to consider the tasks of audit inspection, investigations and discipline, auditor approval and continuing professional development and the setting of technical and ethical standards for statutory audits and auditors.

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?

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?

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?

☒ Yes ☐ No ☐ Not sure ☐ Not applicable

See response to Q9.

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 be needed to ensure that authority only retained responsibilities or reclaimed delegated responsibilities in appropriate circumstances? What do you consider these circumstances should be?

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.

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[3]?

☐ Yes ☐ No ☐ Not sure ☐ Not applicable

If so, which body or bodies do you think should have statutory powers for the removal of statutory auditors from the register?

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?

☒ Yes ☐ No ☐ Not sure ☐ Not applicable

See response to Q9.

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?

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?

☒ Yes ☐ No ☐ Not sure ☐ Not applicable

We believe that the cap of 70% on non-audit services should not be reduced. Audit firms are currently subject to performance and ethical standards to ensure permissible non-audit services do not introduce independence conflicts. We believe any reduction could result in the creation of 'pure audit firms' which we do not support. We have concerns that such firms may not be able to attract staff of a suitable quality because of the lack of opportunity offered by such firms compared to multidisciplinary firms, with a consequent adverse impact on audit quality.

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?

[3] The Statutory Auditors (Registration) Instrument 2008 currently applies for this purpose, having been made by the FRC using powers in section 1239 of the Companies Act, which are delegated to it.

In our view, it would be beneficial to include a definition for the terms 'statutory audit fees' and 'non-audit fees' as this will reduce the risk of incorrect classification.

In addition, 'other assurance services' are referred to in the introductory text of the Regulation. It would be helpful to provide guidance as to what services would be envisaged as 'other assurance services'. For example, listing rules may require auditors to review half-yearly financial statements or circulars that form part of the capital raising process. We would not propose a 'white list' approach but believe guidance as to what constitutes such services will help ensure consistent classification.

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.

☒ Yes ☐ No ☐ Not sure ☐ Not applicable

The FRC should be capable of applying the 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 as FRC's Ethical Standard 4 currently establishes more restrictive requirements in relation to audit and non-audit services fees received from entities.

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?

☒ Yes ☐ No ☐ Not sure ☐ Not applicable

We support the United Kingdom implementing the exemption from the stipulated threshold on an exceptional basis for a maximum period of two years, which we do not believe should be reduced. The exemption provides PIEs with the flexibility to engage permissible non-audit services so as to benefit from the efficiency of using the knowledge of their statutory auditor without compromising independence, when unusual events and transactions prompt the unavoidable use of the auditor. We believe that the term 'exceptional basis' does not need to be defined as it will vary by entity. Instead the responsibility for approving this cap exemption should rest with the audit committee as they are best placed to determine whether or not 'exceptional' circumstances exist that require this exemption.

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?

☐ Yes ☐ No ☐ Not sure ☐ Not applicable

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?

We do not consider that any further non-audit services should be added to the prohibited list, nor do we support the 'white list' approach as it risks further restricting the audit committee's ability to determine the most qualified audit firm for specific services to be provided. Also, proposed services may not always be easily classified into one of the allowable services groupings and would thereby create the potential for misinterpretation. We believe there are other safeguards in place to mitigate threats to independence such as all non-audit services requiring approval from the audit committee (after having assessed the threats and safeguards to auditor independence). Further, the list of prohibited non-audit services in Article 5 is more extensive than the rules set out in Ethical Standard 5.

We support the Member State option in Article 5.3 of the Regulation as it is appropriate to allow the provision of services that have no direct or have immaterial effect, separately or in aggregate, on the audited financial statements. We believe that where these conditions are met, the audit committee should be empowered to monitor and approve such services without regulatory restrictions. Also, audit firms are already subject to performance and ethical standards to ensure that non-audit services do not introduce independence conflicts.

The definition of 'no direct or have immaterial effect on the audited financial statements, either separately or in the aggregate' could benefit from further clarification. In particular, we recommend applying the derogation to allow investor tax reporting that is required to distribute UK domiciled investment funds in other EU countries as this service has no impact on the 'audited financial statements' of the fund or manager and should, in our view, be a permissible service.

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:

- underpin the standards? And,
- introduce simplifications for audits of small non-PIEs?

Please provide further information to support your answer.

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?

☒ Yes ☐ No ☐ Not sure ☐ Not applicable

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 as it provides more information to shareholders to assist them to understand the extent of non-audit services provided by auditors and the amount of non-audit fees paid to auditors to aid in evaluating auditor independence.

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?

(b) the additional costs associated with reallocating some of the non-audit services that would otherwise have been provided by the same statutory auditor?

(c) the extent to which these additional costs vary by the size of PIEs?

(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?

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?

☒ Yes ☐ No ☐ Not sure ☐ Not applicable

We believe that, for practical purposes, the alternative systems for the appointment of an auditor in certain circumstances as set out in the Companies Act 2006 should continue to operate in the United Kingdom 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?

Q28. Where the PIE is exempted from having an audit committee (e.g. 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?

☒ Yes ☐ No ☐ Not sure ☐ Not applicable

We agree that in situations where the PIE is exempted from having an audit committee, the board of directors, being the collective body charged with responsibility for governance, should determine the recommendations that should be put to shareholders of the audited entity on appointment of auditors.

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?

☐ Yes ☒ No ☐ Not sure ☐ Not applicable

BlackRock do not support joint audits, which would duplicate efforts and result in additional costs. To the best of our knowledge, joint audits have not improved audit quality and may instead reduce audit quality because of the inherent difficulty in coordinating complex, global engagements and the potential risks associated with overlapping responsibilities between two auditor firms. In addition, the company's management would spend additional time communicating issues and responding to duplicative procedures. However, where joint auditors are to be used we would support them being appointed on the basis of a retender.

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 ☐ No ☐ Not sure ☐ Not applicable

We support this extension. We believe that audit risk is highest during the first few years after an auditor transition. Therefore, setting the duration to a shorter period of time would not, in our view, allow an audit firm to develop institutional knowledge or gain an in-depth understanding of areas of greater risk. In addition, a shorter duration would lead to a reduced incentive for audit firms to invest in the audit relationship resulting from the cost of tendering which would ultimately be passed to investors.

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 ☐ Not sure ☐ Not applicable

b) when the audit engagement was last retendered?

☒ Yes ☐ No ☐ Not sure ☐ Not applicable

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 ☐ Not sure ☐ Not applicable

d) the directors' reasons for considering that the proposed year is in the best interests of the company's members?

☒ Yes ☐ No ☐ Not sure ☐ Not applicable

Do you consider that any other information should be included in addition the above? Please provide further information to support your answer.

☐ Yes ☒ No ☐ Not sure ☐ Not applicable

On the basis of transparency, we agree with the proposal that the PIE'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.

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?

☐ (a) ☒ (b) ☐ (c) ☐ No preference ☐ Not applicable

For the reasons detailed in our response to question 30, we believe the next tender process in such a situation should be held after a further 10 year-period has expired (i.e. year 17 in this example). However, clarity should be provided on the maximum permissible audit duration so that the audit engagement could then continue for a maximum duration of up to 20 years following a public tender in year 17. Audit committees should not be discouraged from tendering because of a forced reduction in the overall audit tenure of 20 years.

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?

We believe that the sanctions should be applied in cases where the retendering and rotation framework has been breached by the PIE and its auditor should be proportionate and reasonable with flexibility to remedy the breach within an established timeframe.

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?

As detailed in our response to question 30, we believe that there are significant costs associated with increased frequency of tendering and rotation. These costs would be borne by both audit

firms and PIEs and ultimately passed on to investors.

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?

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.

☒ Yes ☐ No ☐ Not sure ☐ Not applicable

We 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) as it would improve communication between auditors and shareholders, investors, creditors and potential investors and creditors as well as with audit committees.

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?

☐ Yes ☐ No ☐ Not sure ☐ Not applicable

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)?

☒ Yes ☐ No ☐ Not sure ☐ Not applicable

We 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) (ISAs) as it would improve communication between auditors and shareholders, investors, creditors and potential investors as well as with audit committees.

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?

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?

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)?

☒ (a) ☐ (b) ☐ (c) ☐ No preference ☐ Not applicable

We believe that the small companies audit exemption thresholds should remain aligned with those for the small companies accounting regime.

Chapter 5

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?

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?

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 ☐ No ☐ Not sure ☐ Not applicable

We agree that the implementation of EU requirements on technical standards should be primarily through changes to the FRC's ISAs (UK and Ireland) as the majority of the new requirements are already contained in existing UK auditing standards.

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 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?

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?

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 ☐ Not sure ☐ Not applicable

We agree that following any adoption of ISAs by the European Commission, the FRC should have the discretion to apply standards where the Commission has not adopted an ISA covering

the same area, subject to appropriate consultation and due process.

(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 ☐ Not sure ☐ Not applicable

We agree that following any adoption of ISAs by the European Commission, the FRC should have the discretion to 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, subject to appropriate consultation and due process.

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)?

We have concerns that Article 5.4 in the Regulation implies that the PIE's audit committee (or the group audit committee acting on behalf of the PIE) would have to pre-approve all permissible non-audit services provided by the statutory auditor (including its member firms) even if they are to be provided to non-EU parent entities or non-EU controlled undertakings. We understand that the European Commission's September 2014 Q&A in relation to an analogous question "*What if the audit client has subsidiaries which operate in different jurisdictions (EU and non-EU) which are required to apply different auditor rotation rules?" clarified that "The Regulation does not have any extraterritorial effects – it applies to PIEs that operate within the EU only. Thus, if a PIE incorporated in the EU has a subsidiary incorporated in a third country, there is no legal obligation upon this PIE to rotate its auditors in this third country, unless the law of the latter states so."*[4] Applying this by analogy would result in the PIE's audit committee having a duty to pre-approve non-audit services for controlled undertakings of the PIE and its parent within the EU, not those outside the EU. This is consistent with our interpretation of the legislation but we would welcome this being clarified by BIS.

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?

[4] The European Commission's Q&A is available here: http://ec.europa.eu/internal_market/auditing/docs/reform/140903-questions-answers_en.pdf

See response to Q48 above.

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?

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?

☐ (a) ☐ (b) ☒ (c) ☐ No preference ☐ Not applicable

We agree that the single competent authority (the FRC in the UK) with responsibility for regulation of audit should receive the information required to be provided to supervisors of PIEs, i.e. the Prudential Regulatory Authority for banks, building societies and insurers and the Financial Conduct Authority for other PIEs so that it can perform effectively as the single competent authority.

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?

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?

☐ Yes ☐ No ☐ Not sure ☐ Not applicable

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;

(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?

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