



Chris Hodge
Financial Reporting Council
Aldwych House
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Dear Chris

CHOICE IN THE UK AUDIT MARKET, PROGRESS REPORT AND FURTHER CONSULTATION

Issued for comment by the Financial Reporting Council

ACCA (the Association of Chartered Certified Accountants) welcomes the opportunity to comment on the above progress report (the paper). We are pleased to continue to participate in the public debate about the audit market for public interest entities and also to have responded to significant consultations on matters having an impact in this area, such as transparency reporting by auditors and revised guidance for audit committees.

ACCA is the largest and fastest-growing global professional accountancy body with over 122,000 members and 325,000 students in 170 countries. We aim to offer the first choice qualifications to people of application, ability and ambition around the world who seek a rewarding career in accountancy, finance and management. ACCA works to achieve and promote the highest professional, ethical and governance standards and advance the public interest.

In the appendix to this letter we set out our comments in three sections, as requested in the paper.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Allen Blewitt'.

Allen Blewitt

APPENDIX

Changes to audit firm ownership rules

Recommendation of Market Participants Group

'The FRC should promote wider understanding of the possible effects on audit choice of changes to audit firm ownership rules, subject to there being sufficient safeguards to protect auditor independence and audit quality.'

Invitation to Comment

To promote debate, the FRC invites comments on this discussion paper to be published on the FRC's website. Views are sought, in particular, on the completeness and accuracy of the analysis, and any additions or clarifications that could be useful.

As Appendix 1 to the paper sets out, promotion of a wider understanding has apparently been restricted to the issue of the current consultation. In the absence of information on the distribution of the paper and other communication efforts of the FRC, it is arguable whether this amounts to any effective widening of those with an understanding of the issues. Instead, the paper seems to us to concentrate on improving the depth of understanding of what is a difficult area.

The Recommendation was worded in terms of the possible effects on audit choice but the analysis includes the potential effects on audit quality. We agree with this approach as audit quality should not be compromised by measures aimed at increasing choice. The analysis includes several sections where a risk is presented in conjunction with existing mitigating factors but no conclusions are drawn as to whether (were it to be permitted) a major equity investment (for example, seeking a listing) could be effectively safeguarded and hence what further measures might be necessary. Although this might be regarded as more in the way of speculation, we are unsure how the FRC could *'use the discussion paper to influence (rather than inform) legislative change in the European Union and the US'* unless it had taken a view on such issues. This raises the question as to whether the FRC should be seeking change at all.

In general we are not convinced that capital structure reform will have any substantial impact on the development of the audit market. This is partly because of the greater impact of other factors and partly because inward investment can be obtained by Big Four and non-Big Four auditing firms alike. As set out in the analysis, there are even concerns that the Big Four firms could use external capital to make the barriers to entry for other firms even higher.

Use of firms from more than one network

Recommendation of Market Participants Group

'The FRC should provide independent guidance for audit committees and other market participants on considerations relevant to the use of firms from more than one audit network.'

Consultation

Views are sought, in particular, on:

- *Whether the guidance fairly reflects the circumstances in which groups may find it useful to consider each group audit arrangement (firms from a single network, firms from more than one network and joint auditors).*
- *Whether the guidance fairly reflects the factors that audit committees may wish to consider for each group audit arrangement.*

In preparing this draft guidance, the FRC has taken a direct step towards compliance with the Recommendation. The guidance will form part of the FRC's corporate governance guidance relevant to audit committees and we assume that, in order to properly inform other market participants, further steps will be taken to disseminate it more widely.

The paper notes that the draft guidance describes considerations relevant to the use of firms from one audit network as well as those relevant to the use of firms from more than one network. It is important to stress that auditing standards, quality control standards and ethical standards apply equally whatever audit firms are engaged.

We suggest that the provision of balanced guidance does not accord with the spirit of the Recommendation, which was intended to address a perceived barrier to auditor choice through the independent communication of relevant facts. Indeed, beginning the guidance with *'Use of firms from a single network'* and commencing *'Most groups choose to appoint one firm to audit the parent group and the consolidated group accounts.'* could be seen as the beginning of an argument for the merit of the status quo. While joint appointments and audit arrangements involving firms from more than one network may present efficiency and accountability challenges, such arrangements should be facilitated.

The guidance on *'Use of firms from more than one network'* has been written in a manner that could be interpreted as seeking to dissuade such arrangements. It begins *'In some circumstances it may be possible to achieve a high quality and cost-effective audit by using firms from more than one network.'* The implications are that it is only possible in some restricted circumstances and that a good audit is not certain (*'may be possible'*). There is a list of only three circumstances *'for which this arrangement may be useful'*. Matters audit committees may wish to consider are presented as questions about perceived difficulties.

Similar criticisms could be levelled at the way material on *'Use of joint auditors'* is presented. No attempt has been made to present arguments raised by those favouring joint audits that *'two heads are better than one'* such that audit quality is enhanced, as indeed is the ability of a group to withstand the withdrawal of one of its auditors from the market place.

Other aspects of progress with the implementation of the MPG's Recommendations

In this section of our comments we deal with certain of the MPG recommendations which remain relevant from our perspective as an accountancy body. We do so in the order in which they are presented in Appendix 1.

2: Audit firms should disclose the financial results of their work on statutory audits and directly related services on a comparable basis.

We are disappointed with progress in this area as relevant firms will have the basic accounting data already.

3: In developing a policy on auditor liability arrangements, regulators and legislators should seek to promote audit choice, subject to the overriding need to protect audit quality.

The issue of audit quality has been much to the fore in relation to auditor liability limitation agreements but the related promotion of auditor choice has been much less visible in the UK (no explicit mention in FRC guidance on auditor liability limitation agreements) than elsewhere, for example in the EC Recommendation of 5 June. It may be that the FRC could adopt a higher profile in communicating this MPG recommendation in relation to auditor liability as it has application in many jurisdictions.

4: Regulatory organisations should encourage participation on standard setting bodies and committees by appropriate individuals from different sizes of audit firms.

We welcome the communication with IFAC Boards and Committees and agree wholeheartedly that professional diversity is an important component of regulatory credibility.

With regard to the FRC itself, and in particular the Auditing Practices Board, we acknowledge that there is effective contribution from non-Big Four firms (and indeed SMPs) through sub-committees and working parties. We would hope to see more non-Big Four members of the APB itself in due course as that is where market perception of effective participation is focussed.

5: The FRC should continue its efforts to promote understanding of audit quality and should promote greater transparency by the firms and the FRC of the capabilities of individual audit firms.

Following the successful issue of the paper on the drivers of audit quality and the Regulations on transparency reports, we look forward to the outcome of Professional Oversight Board monitoring of how firms respond to these challenges.

14: Every firm that audits public interest entities should comply with the provisions of a Combined Code-style best practice corporate governance guide or give a considered explanation.

We are concerned that the timetable for development of a 'Combined Code-style best practice corporate governance guide' does not seem to allow for the normal length of public consultation that we would expect for a matter of this nature. The FRC will be aware of the potential global impact of this development and we suggest that significant effort should be made to solicit input from a wide range of stakeholders.

Recommendations 8,9 12 and 15.

We have responded separately in respect of aspects of revised guidance for audit committees (the Smith Guidance) and await the final guidance in due course.