



# Grant Thornton

Our Ref NJJ/SAM/0308  
Your Ref FRC PLAN & BUDGET 2008/09

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Dear Sirs

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## Financial Reporting Council Draft Plan & Budget 2008/09

We are pleased to comment on the Financial Reporting Council's (FRC) draft plan and budget covering what we know will be a challenging period for the capital markets and the audit profession in 2008/09

We strongly support the FRC's practice in publishing its draft plan and budget. By being seen to take account of the views of market participants, the FRC increases the chance it will continue to attract broad support for its work and outputs.

### Key themes

While the risk is identified in the body of the paper, in our view recruitment and retention of audit talent is a major risk for the capital markets and should be an associated FRC priority for the coming period. In our view the long term future of the audit profession is at risk if the imbalance between risk and reward is allowed to continue. The FRC is ideally placed to reverse that trend by embarking on a program of measures to address that imbalance. Audit quality is only as sustainable as the people conducting audits.

Clearly UK business is on the verge of a difficult period, and it is right that the regulator takes a strong interest in conduct of audit firms and auditing. In our view there is a chronological order to auditor and auditor oversight reaction to the business climate:

- the FRC publishes its views on risk areas to focus the work of companies and auditors (which the FRC has dealt with appropriately)
- companies and auditors are given the opportunity to demonstrate appropriate action in light of the business climate
- after the event there is debate about actions taken and lessons to be learned

In our view the FRC should avoid the risk of distracting the attention of companies and auditors from key issues if it embarks on a detailed debate about the potential outcome of the current audit cycle.

It is important that the UK and European voice is heard at international debates, and we would encourage the FRC to publish as part of future FRC plans those international projects where FRC bodies intend commit resource.

### Major projects

We note the project to "review the complexity and relevance of current reporting

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requirements". This is an extremely wide-ranging topic, and one where in light of IAASB and IASB committed work plans through 2009 we doubt whether workable solutions will accrue from the project in the short or medium term. We also question whether this is a project that the FRC should undertake on its own, when a lone UK voice might not carry as much weight as a group of cross-border voices, though clearly the FRC's voice should be heard in such cross-border discussion.

### **FRC proposed expenditure**

Most market participants will agree that the climate in 2008 and 2009 will be more challenging. However, we question whether an appropriate response from the regulatory body at this time is to increase their budget by 9%. There is logically a time delay between a difficult reporting climate and the need for additional oversight resource. AIM and PLUS companies, who contribute for the first time this year through the FRC's business levy, might also question the benefit they receive when the major projects identified by the FRC are of less direct interest to them and their investors.

In addition to core operating costs we note the budgeted increase for audit inspection costs of 23%. In our view, the paper does not sufficiently make the case for the budgeted increases, which sends the wrong message to market participants. A balanced case for additional funds could avoid the unintended signal that audit quality is in decline, or that the auditor oversight process has not previously had sufficient resource to fulfil its statutory responsibilities.

The draft plan refers in the main to increased workload of the FRC's bodies, , but there are limited comments on efficiency. FRC commitments on efficiency might accrue from the audit inspection process. A reader might look to the Auditing Practices Board and the Accounting Standards Board whose responsibilities appear to be reduced now that international standards are increasingly accepted.

We note the government's stated intention to withdraw funding to the FRC in 2009. We will respond in more detail on the issue of the Accountancy Scheme Review to the Accountancy and Actuarial Discipline Board consultation paper. However, for completeness we note here that the FRC's explanations for potential increases in AADB costs largely indicate the need for central funding, as opposed to the proposed ad hoc increases to levies on companies and auditors.

If you have any questions on this response, please contact Steve Maslin (phone: 020 7728 2736; email [Steve.Maslin@gtuk.com](mailto:Steve.Maslin@gtuk.com)) or Nick Jeffrey (phone: 020 7728 2787; email [Nick.Jeffrey@gtuk.com](mailto:Nick.Jeffrey@gtuk.com)).

Yours faithfully

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## **Appendix - Grant Thornton responses to specific questions raised in the consultation paper**

### **Our new approach to explaining our priorities**

**Question 1:** Will the approach we have developed provide a clearer view of the judgements we have made and be helpful in obtaining better feedback on our assessments?

**Grant Thornton response:** Yes. We expect this to be reflected in an increased number of responses to this year's draft plan and budget.

**Question 2:** Will the publication of our assessments be helpful in highlighting the priority areas for action to contribute to the achievement of the outcomes defined in the Strategic Framework?

**Grant Thornton response:** Yes. The publication of assessments helps participants to understand how the FRC developed their proposals, and helps to inform feedback on the draft plan and budget.

### **Our assessment of major risks**

**Question 3:** Do you agree that our assessment of the achievement of the outcomes in our Strategic Framework, in the downside scenario, properly reflects the plausible risks?

**Grant Thornton response:** In general yes, but see our response to question 4.

**Question 4:** Do you have any comments on the detailed assessments of the risks to the achievement of the outcomes in our Strategic Framework included in our document Draft Plan 2008/09: Supplementary Information published on our website? Is there additional evidence which should be considered in relation to these assessments?

**Grant Thornton response:** We make the following comments of detail on risks identified in the paper:

- corporate governance - the way the words are phrased implies that improved disclosure of corporate governance arrangements will improve standards of performance. In our view better disclosure might improve shareholder understanding of the board's procedures but in itself will not enhance standards of conduct
- professionalism of accountants and actuaries - we question whether there is a plausible risk that the accountancy bodies will not address issues on professionalism of their members
- FRC effectiveness - in our view collectability of funds is not the primary risk, but the case for central funding is strongest in relation to the work of the Accountancy and Actuarial Discipline Board

**Question 5:** Are there any other outcomes in our Strategic Framework where you believe there are significant concerns or serious shortcomings in the downside scenario which we have not identified? Please explain the risks which have led you to believe this.

**Grant Thornton response:** A question not asked is whether participants agree with the strategic framework. In our view, outcome three Auditing as described does not adequately support the overall aim to promote confidence in corporate reporting and governance. In particular, outcome three does not address the fundamental need of capital markets for a sustainable and robust audit profession. A particular risk for the capital markets of the future is failure to recruit and retain sufficient quality and quantity of audit talent, which is

identified as a risk under outcome 5 but is not given the prominence that it merits as a key theme of the work programme.

**Proposed major activities and projects and assessment of residual risks**

**Question 6:** Do you have any comments on the scope and relevance of the proposed major activities and projects included in the Draft Plan for 2008/09?

**Grant Thornton response:** We have nothing to add to the comments in our covering letter.

**Question 7:** Do you have any comments on the more detailed list of activities and projects set out in the document Draft Plan 2008/09: Supplementary Information which we have published on our website?

**Grant Thornton response:** We have nothing to add to the comments in our covering letter.

**Question 8:** Are there any additional activities or projects which should be included in the Plan for 2008/09 or for future years?

**Grant Thornton response:** We have nothing to add to our comments in our covering letter.

**Question 9:** Do you agree with our assessment that there are significant concerns even in the upside scenario about the achievement of the outcome defined in the Strategic Framework in relation to an efficient market for audit services in the UK?

**Grant Thornton response:** We agree that there are concerns about the public company audit market, but we disagree with the paper's focus on the largest four audit firms. The issue is not primarily about preventing the collapse of a big four firm, because no firm is too large to fail. The solution is primarily about preventing the collapse of any firm for no good reason, together with encouragement of market-led solutions to increase choice in the public company audit market.

**Question 10:** Do you have comments on the detailed assessments of the upside scenarios set out in our document Draft Plan 2008/09: Supplementary Information?

**Grant Thornton response:** In outcome 3 Auditing, we would encourage the FRC to do more than monitor implementation of the Market Participant Group's recommendations. In particular, there are implementation arrangements that we believe the FRC has committed to in 2008, including revised guidance for audit committees (the Smith Guidance), and guidance for audit committees and other market participants on considerations relevant to the use of firms from more than one network.

**Question 11:** Are there any other outcomes in our Strategic Framework where you believe there are significant concerns or serious shortcomings in relation to the upside scenario which we have not identified?

**Grant Thornton response:** No.

**Expenditure**

**Question 12:** Do you have any comments in relation to our draft Budget proposals for 2008/09?

**Grant Thornton response:** We have nothing to add to our comments in the covering letter. In general, we do not believe that the case has been sufficiently made for the budgeted increases, particularly the significant increase suggested in audit inspection costs.