



Mr C Hodge
Financial Reporting Council
Fifth Floor
Aldwych House
71–91 Aldwych
London WC2B 4HN

Ref: TECH-CDR-778

6 June 2008

Dear Mr Hodge,

**Financial Reporting Council
Consultation on proposed changes to guidance on audit committees (the
Smith Guidance)**

I write to convey ACCA's views on the FRC's consultation on proposed changes to guidance on audit committees (the Smith Guidance) to help implement FRC proposals on audit choice. Our views reflect discussions on the subject by our Corporate Governance and Risk Management Committee and our Auditing Committee.

General comments

We believe that the Smith Guidance is a valuable resource to audit committees and we are content that no major changes are being proposed.

We acknowledge that large listed companies have many reasons to choose one of the 'Big Four' audit firms. Even if a large company wishes to consider a smaller audit firm, the smaller firm may be reluctant to take on the work. One reason is a firm could find it harder to meet independence requirements as there may be a self-interest threat where an audit partner is employed principally on that audit engagement.

It was felt that the FRC proposed changes to the Smith Guidance would not, in themselves, help audit choice. We recognise however that, with other measures, they could play a part in increasing choice.

Specific Comments

We have the following comments on specific amendments proposed in the consultation:

Re 4.21

[New] 4.21 The audit committee should assess periodically the risks associated with the possible withdrawal of their external auditor from the market and consider whether any mitigating action is appropriate.

We note that the FRC believes this provision would not add to the regulatory burden yet it was not clear how an audit committee should assess these risks or what mitigating action might be possible. It seems likely that, in practice, such assessment and consideration would be a limited process. We accept that nevertheless this could have some value and, in particular, could serve to raise the issue in the minds of audit committee members. Our understanding is that companies had little difficulty finding an auditor following the demise of Andersen but Andersen had few large listed clients and the firm's staff mostly found jobs with other firms that had taken on Andersen work. A withdrawal from auditing by, for example, PwC would, however, create a gap that may be harder to fill.

Having regard to possible problems with independence where non audit services are concerned, a prudent audit committee may decide to identify one of the 'Big Four' firms with whom it will place no work at all in case it needs to choose a new auditor at short notice. The withdrawal from audit by a 'Big Four' firm may however provide a stimulus for companies to choose an auditor from outside what was the 'Big Four'.

We assume that, whatever assessment and consideration an audit committee may do in this respect, the FRC will also periodically assess the risk of withdrawal from auditing by a large firm and advise companies accordingly. The FRC would be better placed to assess these risks than would individual audit committees.

Re a new section 4.22:

[New] 4.22 The audit committee report should explain to shareholders how it reached its recommendation to the board on the appointment, reappointment and removal of the external auditors. This explanation should normally include:

- any contractual obligations that acted to restrict the audit committee's choice of external auditors;***
- when the audit was last subject to tender; and***
- when the current group auditor was appointed.***

Tender is one way of assessing competitiveness. We suggest that it would be better to ask for disclosure on when the audit was last subject to a 'competitive process'. This would mean that other competitive processes such as benchmarking can be disclosed as well as tender.

Re 4.27

4.27 The audit committee should monitor the external audit firm's compliance with applicable United Kingdom ethical guidance relating to the rotation of audit partners, the level of fees that the company pays in proportion to the overall fee income of the firm, ~~office and partner~~, or relevant part of it and other related regulatory requirements.

The words 'or relevant part of it' are ambiguous and would benefit from clarification. We believe that the intent of the MPG's recommendation is for audit committees to consider factors other than the level of fees in proportion to the overall fee income of the firm, in particular those set out in APB Ethical Standard 4. To that end the guidance should be more closely aligned to the ethical standards to allow audit committees to assess the threats and evaluate the safeguards.

Re 5.2

5.2 The audit committee section should include, inter alia:

- a summary of the role of the audit committee;
- the names and qualifications of all members of the audit committee during the period;
- the number of audit committee meetings;
- a report on the way the audit committee has discharged its responsibilities; *and*
- *the explanation provided for in paragraph 4.29 above. a summary of the audit committee's policy on non-audit work provided for in paragraphs [4.29] and [4.32] above; and*
- *an explanation of the audit committee's recommendation on the appointment, reappointment and removal of the external auditors provided for in paragraph [new] 4.22 above.*

We note that companies can form their own interpretation of what is meant by a 'policy on non audit work'. Companies may not wish to disclose financial limits and disclosure is likely to be anodyne.

Re the proposed change to 2.4 of the Combined Code.

2.4 The chairman of the company should not be an audit committee member. In FTSE 350 companies all members of the committee should be independent non-executive directors. The board should satisfy itself that at least one member of the audit committee has recent and relevant financial experience

We consider that the words 'recent and relevant financial experience' need greater definition. Financial experience is not necessarily accounting experience and, in our view, accounting experience is necessary. We therefore recommend that the wording should change to *'The board should satisfy itself that at least one member of the audit committee holds an accounting qualification (such as CCAB or equivalent international qualification) and has recent and relevant accounting experience'*.

Please let me know if you have any questions on, or would like to discuss, any of our comments above.

Yours sincerely



Paul Moxey
Head of Corporate Governance and Risk Management