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For the attention of Mr Chris Hodge

6 June 2008

Dear Sirs

Consultation on proposed changes to guidance on audit committees (The Smith Guidance)

We write in response to the invitation to comment on the proposed changes to the Smith Guidance for audit committees. We have reviewed the proposed changes in the context of the recommendations made by the FRC's Market Participants Group (MPG), revisions proposed to the 2006 Combined Code and the APB's Ethical Standards.

We support the changes proposed in respect of MPG recommendations 9, 12 and 15. We have concerns regarding the interpretation of MPG recommendation 8 and the resulting new paragraph 4.22 of the Smith Guidance.

MPG recommendation 8 is that the FRC should amend the section of the Smith Guidance dealing with communications with shareholders to include a requirement for the provision of information relevant to the auditor selection decision. The new 4.22 includes three bullet points. The first specifically addresses MPG recommendation 9 regarding the existence of any contractual obligations that act to restrict the audit committee's choice of external auditor. We support this change. However, the second and third bullets represent the FRC staff's interpretation of "information relevant to the auditor selection decision". We argue that this goes against principles-based standards setting and goes beyond the spirit of the MPG recommendation. We also question why the FRC chose to select these two elements as specific requirements relevant to the auditor selection decision. In our view more relevant information would be matters such as quality, independence and objectivity.

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Introducing a requirement for audit committees to disclose when the audit was last subject to tender will result in this being sole metric on which the auditor selection decision is based. This is effectively mandatory auditor rotation by another route. Mandatory auditor rotation has consistently been rejected as a means to improve competition and choice in the UK audit market. The European Commission and Parliament also gave much consideration to the Bucconi academic research into mandatory rotation of firms and concluded that it is not appropriate. In addition the corporate community is firmly against such a move on the grounds of cost.

We suggest that the new 4.22 is drafted as follows:

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 include details of any contractual obligations that acted to restrict the audit committee's choice of external auditors.

Regarding the changes based on the 2007 Review of the Combined Code set out in section 3, we do not believe that the proposed change to paragraph 2.3 accurately reflects the proposed revision to the Combined Code. The FRC is proposing that Code provision C.3.1 should include the following sentence: "In smaller companies the company chairman may be a member of, but not chair, the committee in addition to the independent non-executive directors, provided he or she was considered independent on appointment as chairman". The words underlined have been omitted from the proposed change to the Smith Guidance. This is an important element of the Code change as it preserves the independence of the audit committee. We believe that these words should be included in the Smith Guidance.

If you would wish to discuss these comments further with us, please contact Martyn Jones (mjones@deloitte.co.uk) or Tracy Gordon (trgordon@deloitte.co.uk).

Yours faithfully



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