

04 July 2007

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Dear Mr Rose

**Choice in the UK audit market: interim report of the Market Participants Group**

Thank you for the opportunity to comment on this interim report. CIMA has over 158,000 members and students in 161 countries who work across all business sectors. As CIMA members cannot conduct statutory audits, we are pleased to participate in this project from a business perspective and we are of the firm opinion that the best solutions will only arise from a consensus of all the participants in the financial reporting process.

CIMA would first like to commend the FRC for its approach to this project which we believe could stand as a model for consultations in the future. In particular, we would like to express appreciation for its efforts to pull together the Market Participants Group and to gain input from as broad an audience as possible through the stakeholder meetings and other presentations together with the production of a well-presented interim report.

We are strongly supportive of the market-based approach to the issue and we welcome the package of pragmatic and proportionate recommendations, all of which we support. We are very pleased that the FRC is taking a leading role on this issue on the global stage and we would strongly support its efforts to achieve global solutions. Our comments on specific provisional recommendations follow.

**Provisional recommendation 1** - 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.

This is potentially the most powerful recommendation. CIMA believes that there is a case for liberalising the audit firm ownership rules subject to appropriate safeguards and preferably accompanied by liability reform. The principle of divorcing effective regulatory requirements from ownership structures is well-established in many other industries and it should be workable within the audit industry. However, the main obstacle to this recommendation is whether and how quickly it could be implemented. It could be many years before we are in a position to judge the overall efficacy of the proposed measures if they are progressed further.

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

CIMA believes that it would be useful to see information relating to the wider audit segment of the firm together with information relating to statutory audit and directly related services. Given the

nature of the industry in which the audit firms operate, we believe that they should demonstrate current best practice in all aspects of business reporting, both financial and non-financial. One such example of emerging best practice is provided by the Report Leadership project in which CIMA is an active participant. Further details, including a downloadable brochure can be found at [www.reportleadership.com](http://www.reportleadership.com) and CIMA would be very pleased to discuss the report further if the MPG would find it helpful.

**Provisional recommendation 3** - In developing and implementing policy on auditor liability arrangements, regulators and legislators should seek to promote audit choice, subject to the overriding need to protect audit quality.

No additional comments.

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

This is a useful recommendation in that it should be straightforward to implement and could have a powerful impact in terms of improving the market perception of non-Big Four firms. We believe that these firms should find it a worthwhile investment of their time.

**Provisional recommendation 5** - The FRC should continue its efforts to promote understanding of audit quality and should promote greater transparency of the capabilities of individual audit firms.

No additional comments.

**Provisional recommendation 6** - The accounting profession should establish mechanisms to improve access by the incoming auditor to information relevant to the audit held by the outgoing auditor.

As we pointed out in our earlier response, it would be useful to have some form of mechanism or code of best practice to facilitate auditor change. We agree that this is a straightforward proposal to implement.

**Provisional recommendation 7** - 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.

We endorse the need for audit committees to be able to make decisions as to whether to use a single global network or not on a well-informed basis. We agree that, in principle, there is no reason why companies should not use firms from more than one network. CIMA therefore believes that this is a sensible recommendation in that it will improve information available to audit committees, while still giving them the freedom to make the decision that is best suited to their particular circumstances.

It will be interesting to see what impact this guidance will have on decisions. We would suggest that, in due course, if the guidance proves to have little impact, consideration could be given to requiring audit committees to disclose the reasons for their choice of single networks – although this could form part of provisional recommendation 8.

**Provisional recommendation 8** - 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 re-selection decision.

We support this proposal as an effective means of enhancing dialogue with investors.

**Provisional recommendation 9** - When explaining auditor selection decisions, Boards should disclose any contractual obligations to appoint certain types of audit firms.

No additional comments.

**Provisional recommendation 10** - Investor groups, corporate representatives and the FRC should develop good practices for shareholder engagement on auditor appointment and re-appointments and should consider the option of having a shareholder vote on audit committee reports.

We support this proposal as an effective means of enhancing dialogue with investors.

**Provisional recommendation 11** - Authorities with responsibility for ethical standards for auditors should consider whether any rules could have a disproportionately adverse impact on auditor choice when compared to the benefits to auditor objectivity and independence.

No additional comments.

**Provisional recommendation 12** - The FRC should review the Independence section of the Smith Guidance to ensure that it is consistent with the relevant ethical standards for auditors.

No additional comments.

**Provisional recommendation 13** - Regulators should develop protocols for a more consistent response to audit firm issues based on their seriousness.

We believe that this recommendation would constitute a useful first step towards ensuring as much consistency amongst regulators as possible.

**Provisional recommendation 14** - Every firm that audits public interest entities should comply with the provisions of the Combined Code on Corporate Governance with appropriate adaptations or give a considered explanation if it departs from the Code provisions.

We support this proposal although the FRC will need to provide more clarity as to how the code would be adapted in practice to audit firms. However, we believe that the introduction of non-executive directors to audit firms would be a welcome development and reinforce the importance of audit firms as key public interest entities.

**Provisional recommendation 15** - Major public interest entities should consider the need to include the risk of the withdrawal of their auditor from the market in their risk evaluation and planning.

We support this as an effective market-based approach to this issue. It is important that companies do not rely solely on regulators to mitigate the effects of the withdrawal of a firm although we take it as read that the FRC has its own contingency plans in place.

CIMA believes that this package of measures represents a step in the right direction. However, it is important to regard this project as an iterative process where it will be necessary to review progress on a regular basis and modify recommendations as appropriate in the light of actual experience. We certainly do not regard this as a one-off exercise where complete solutions will be found. As we pointed out earlier, it could be some time before it is possible to judge the efficacy of the proposals.

The next challenge is to develop these proposals further into workable action plans which will fully engage all the market participants effectively. We would strongly recommend that the FRC specifies a timetable for reviewing the action plans and their outcomes on a timely basis.

I trust that these comments will prove helpful in your deliberations and CIMA looks forward to supporting the further progress of this project.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Charles Tilley', is written in a cursive style.

**CHARLES TILLEY**  
Chief Executive