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Mr JEC Grant
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Dear Mr Grant

1. The Institute of Chartered Accountants in Ireland ('ICAI') is pleased to respond to the Financial Reporting Council's Discussion Paper 'Promoting Audit Quality'.
2. We believe the Discussion Paper is a timely contribution to this important topic at a time when financial reporting and auditing, and the general requirements on companies have undergone major change.
3. The Introduction to the Discussion Paper notes that it has been prepared in the context of the financial reporting framework in the United Kingdom and the Republic of Ireland. ICAI welcomes this inclusive approach which is entirely appropriate given the similarities that exist between the financial reporting, auditing, corporate governance and regulatory frameworks in both jurisdictions.
4. ICAI, as a professional body with members based in the UK and Ireland, has found this to be a sensible and pragmatic arrangement in view of the similar regulatory structures that apply in both jurisdictions. We set out below a summary of the principal features of the regulatory structure that currently applies in Ireland.
5. Financial Reporting Standards issued by the Accounting Standards Board are applied by Irish corporates. Auditing standards issued by the Auditing Practices Board ('APB') are followed by auditors who have registration in Ireland. In addition, the company law amendments implementing the Member State options for enabling adoption of International Financial Reporting Standards by the generality of companies contained in Regulation 1606/2002 ('the IAS Regulation') in many respects mirror those implemented by the UK. As regards corporate governance, listed companies in Ireland are required by the Listing Rules of the Irish Stock Exchange to include in their annual report a statement on compliance with the FRC's Combined Code.

6. Like the UK, the Irish Government has introduced measures aimed at strengthening the independent regulation of auditors. In 2000, it established the Review Group on Auditing ('RGA') whose terms of reference included reviewing the then existing regime for regulating statutory auditors making recommendations in relation to this regime, if deemed appropriate.
7. The RGA published its report in July 2000. A direct consequence of this was the Companies (Auditing and Accounting) Act, 2003 ('the 2003 Act') which, among other things, established the Irish Auditing and Accounting Supervisory Authority ('IAASA'). As an independent body, IAASA's role is that of an oversight mechanism in respect of how the professional accountancy bodies supervise their members, particularly in the area of statutory audit.
8. The key functions of IAASA are;
 - The supervision of prescribed accountancy bodies and how they regulate their members;
 - Promoting high standards in financial reporting and auditing;
 - Acting as a source of advice to government on accounting and auditing issues; and
 - Monitoring the accounts of certain classes of companies to ensure compliance with the companies acts.
9. Thus it can be seen, that although different in structural terms, many of the functions of the Financial Reporting Council are also vested in IAASA. In addition, IAASA also observes proceedings at the Accounting Standards Board and the Auditing Practices Board.
10. Responsibility for monitoring the statutory audit of certain public interest entities remains with the recognised accountancy bodies, which activity is in turn overseen by IAASA. We believe this model accords with the particular options available to Member States under the EU 8th Directive in respect of oversight and Quality Assurance.
11. The 2003 Act contains other measures that are addressed in the EU 8th Directive including;
 - A legal requirement for certain entities to establish audit committees;
 - Disclosures relating to remuneration of auditors.
12. Although such requirements are not identical, their direction and purpose are obviously similar to those of the Directive.

13. What is perhaps particularly noteworthy, and arguably different to the current UK regime and that envisaged by the 8th Directive, is that many of the recent measures in Ireland aimed at maintaining audit quality and standards of corporate governance are intended to apply to the generality of companies, with limited exemptions for SMEs, and not just to the public interest sector.
14. As the Discussion Paper acknowledges, therefore, by any measure, there has been *'...a significant amount of change over a short period of time. [Such] changes need to be assimilated by the preparers of financial statements, investors, and audit firms – all of whom must either apply or become familiar with the new requirements'*.
15. While certain differences exist between the structures currently in place in Ireland and the UK, we believe that these are essentially equivalent and are a positive element in the maintenance of audit quality. Both regimes make a positive contribution towards the maintenance of audit quality.
16. Company law in Ireland is kept under review by the Company Law Review Group ('CLRG'), a body established under statute. Further developments in the structure and content of company law are expected as the work of the CLRG progresses. The CLRG is expected to publish soon draft legislation which will consolidate and modernise existing company law. The CLRG has also been requested by government to review particular aspects of the current law with a view to making recommendations on future policy as the consolidated Act and any further amendments required to implement the 8th Directive are considered.

General comments on the Discussion Paper

17. ICAI welcomes the general assertion that the current model in Ireland and in the UK is fundamentally sound and that the combination of recent 'local developments' in both jurisdictions along with any further modifications to these that may result from the EU 8th Directive will serve to maintain and underpin the delivery of high quality audits in Ireland and the UK.
18. One area to which the Discussion Paper might have devoted greater attention is the quality of oversight regimes. Oversight bodies need themselves to contain significant and up to date technical, particularly auditing, expertise and competence. In addition, a sound knowledge of the profession is essential when developing any further practical proposals aimed at improving audit quality. Oversight bodies need to be sufficiently confident to continue to defend the merits of 'principles based' auditing at a time when auditors are faced with an ever increasing body of prescriptive rules. This implies that oversight bodies and their inspection staff need to continue to comprise individuals of the highest calibre who are capable of seeing beyond a 'tick box' approach to monitoring the quality of audits. Not addressing this issue could, we believe, constitute an additional threat to audit quality.

19. An area ICAI particularly welcomes is the reference to the role of audit committees in monitoring audit quality. We support the idea of audit committees becoming more proactive in their dealings with shareholders and would welcome further guidance from the FRC and other relevant bodies on how audit committees might improve on the quality of their communication and their ongoing interaction with shareholders.
20. Our responses to the specific questions raised in the Discussion Paper are in Appendix 1.

Concluding remarks

21. ICAI looks forward to continuing its participation in this ongoing debate and we await the outcome of this consultation process with interest. We have already taken a number of steps aimed at engaging the investor community and other stakeholders in this issue in Ireland and would hope to continue this by engaging in dialogue with interested parties. In the meantime, should you have any queries regarding the content of the response please contact Aidan Lambe, Director, Representation and Technical Policy (Direct line: +353 6377307; Email: aidan.lambe@icai.ie).

Yours sincerely

Aidan Lambe
Director, Representation and Technical Policy

FRC Discussion Paper Promoting Audit Quality

Q.1 Are there other important indicators of an audit firm's culture that are not referred to above?

While we consider that the Discussion Paper has identified the significant indicators of the culture within audit firms, also of importance is the response and reaction of an audit firm to the regulatory environment in which it operates.

Q.2 Are there pressures that could compromise the culture of audit firms that have not been identified above?

From an Irish perspective the pressures caused by sheer economic demand under which auditors now operate is unprecedented. This is a consequence of the rate of increase in economic activity which has occurred in Ireland over the last ten years. There are now significant pressures on audit firms to complete audits as quickly as possible to meet various reporting deadlines imposed on companies. In addition, major changes in requirements of regulatory standards, applicable to audits and audit firms of all sizes, have resulted in auditors spending a large quantity of their audit time demonstrating compliance with such standards. This ultimately has the potential to have a negative impact on audit quality.

Q.3 Are there any further steps that should be taken to build confidence in the culture of audit firms and, if so, what might they be and why are they needed?

Undoubtedly, improvements in transparency as to how audit firms operate and the processes, procedures and independence requirements which govern their conduct should, hopefully, provide users of audit services with additional confidence in these firms. In this regard, the 'transparency report' envisaged by the EU 8th Directive provides an opportunity for firms to improve the understanding of others as to how they operate.

We also consider oversight bodies can play their own role in building confidence in audit firms by being prepared to go on the public record to emphasize the positive aspects of audit firms and the role they play in underpinning confidence in financial reporting.

Q.4 Do you agree that technical skills, personal qualities and practical experience are key drivers of audit quality?

Yes we concur that technical skills, personal qualities, in particular an appropriate level of professional scepticism, and practical experience are key drivers of audit quality.

Q.5 Has this paper identified the issues that could result in an inadequately trained or skilled workforce for audit – if not, what other issues are there and why are they issues?

The pace of economic activity in the Irish market, referred to above, over the previous decade has imposed significant resource concerns for audit firms. This has undoubtedly impacted salary levels and staff retention.

The level of regulatory capture to which auditors are now subjected is undoubtedly also a factor that may result in skilled and experienced auditors deciding against remaining in the audit profession in future. It is incumbent, we believe, on regulators to ensure that they avoid negatively impacting the audit profession to such an extent that it becomes an unattractive career option for individuals of the highest quality.

Of course, the continuation of current inequitable auditor liability regimes is likely to have an increasingly negative impact on the ability of audit firms to retain the brightest and the best.

Q.6 Should there be a fundamental review of the qualification and training requirements for auditors?

We consider that the current regime has served the profession well until now. ICAI itself is responsible for the delivery of training to its students. The quality and content of the education and training that underpins the ICAI qualification has always been high on ICAI priorities. This was recently reinforced by the ICAI's Strategic Review, completed in 2005. ICAI continues to invest heavily in education to ensure that the highest educational standards continue to be observed and that its syllabus remains relevant and appropriate. The additional supervision, including external reviews and assessments, now directed at the profession and the accountancy bodies will undoubtedly continue to ensure that the basic qualification and training continue to be appropriate for the future. Therefore, we see no need for a fundamental review of the audit qualification and training regime.

**Q.7 Are there other factors that determine whether an audit process is effective?
and**

Q.8 Are there threats to the effectiveness of the audit process that have not been identified above?

We concur with the factors and threats identified in this paper. In particular we agree with the assertions relating to over prescriptive auditing standards and regulations. Audit effectiveness and quality will inevitably suffer if auditors are faced with an increased administrative burden in order to demonstrate compliance in a regime that is in danger of becoming essentially rules-based with little or no tolerance for the exercise of professional judgment.

Q.9 Are there further steps that could be taken to counter the threats to the effectiveness of the audit process?

We believe that the regulatory agencies should continue to mount a rigorous and robust challenge to the imposition of overly prescriptive regulatory standards and continue to support principles based auditing.

Q.10 Are there other factors that determine whether audit opinions command confidence?

Yes we believe the following factors may impact on determining whether audit opinions command confidence:

- Audit Committees should be encouraged to be more proactive regarding the effectiveness of the audit process;
- Regulatory authorities should also look at the quality of their own oversight function to ensure that it remains of the highest quality. This paper does not address the quality of regulatory oversight.

Q.11 Are there other reasons why users may not have confidence in the audit opinion?

Yes we consider that a continuing audit expectation gap remains an issue and undoubtedly contributes to a lack of confidence in the audit opinion. There may be merit, therefore, in audit regulators conducting an information/education campaign as to the nature of a statutory audit and what it can and cannot deliver.

This might actually be one positive output of the current consultation process.

Q.12 Are there further steps that could be taken to reinforce confidence in an audit opinion? In particular, what changes to the form and content of the audit report should be considered?

We believe that undoubtedly the style and form of audit reports have become standardised and ‘boiler plate’ in format. There is merit in reviewing and exploring the formats and style of report, and giving consideration to whether changes are needed to the current requirements of auditing standards and existing liability regimes with a view to facilitating the provision of information more specific to the audit undertaken.

Q.13 Are there other external factors that have the potential to adversely affect audit quality?

Yes we believe the following external factors may potentially affect audit quality:

- Probity of Management;
- Clarity of Law and of Accounting Standards;

- Remuneration Structures of Directors and of Management;
- Culture of Management to achieve targets;
- The nature of the audited entity, for example a large subsidiary may be less focused on statutory reporting and more so on other performance drivers;
- Positioning of Financial Reporting process, its freedom from management bias and its willingness to interpret law and standards in a way favourable to company's position; and
- The role and independence of internal audit.

Q.14 Are audit committees discharging their responsibilities in relation to audit adequately and if not, what further steps might be taken to make their role more effective?

At the moment, this is an evolving area in Ireland and we would encourage further initiatives aimed at improving the audit committee effectiveness. In particular we would support further dialogue on this issue between all stakeholders.

Q.15 Should the FRC develop more detailed audit guidance for audit committees to evaluate audit effectiveness? and

Q.16 Should annual reports include a summary of the work undertaken by the audit committee to evaluate audit effectiveness?

Yes, we support the assertion that the FRC and other appropriate bodies should develop more detailed guidance in order to enable audit committees to evaluate audit effectiveness particularly in how they evaluate the audit effectiveness of audit committee and their interaction with the internal audit function.

We also support the assertion that annual reports should include a summary of the work undertaken by the audit committee to evaluate audit effectiveness and also outline the other work which has been undertaken such as for example, the oversight of the financial statements.

Q.17 Are there further steps that should be taken to reduce the risk that these external factors may adversely affect the audit process?

We would support the creation of a forum for ongoing dialogue on audit quality and the monitoring of such. However we consider this should take place on an EU or perhaps a global basis, as opposed to a local and or jurisdictional. This should involve all relevant stakeholders, in particular shareholders. Achieving active shareholder involvement can be problematic. However, we would support FRC and other relevant bodies taking positive initiatives aimed at encouraging active shareholder participation.

We would also encourage audit regulation and the oversight authorities in the publication of their reports to emphasise also the positive aspects of their results rather than merely focusing on the negative aspects.