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Dear Ms Trickett

Reporting on Audit Quality Monitoring - Implementing a New Approach

Deloitte & Touche LLP is pleased to provide a response to the Professional Oversight Board's (**POB**) consultation document: "Reporting on Audit Quality Monitoring – Implementing a New Approach" (*the Consultation Document*)

In September 2006 we responded to the POB's June 2006 consultation document: "Reporting on Audit Quality Monitoring". We considered then, and continue to believe, that there are potential disadvantages and unintended consequences that follow from public reporting in any form. Accordingly, in that response we supported increased public reporting in the form of an extension to the current public report to include a section on a named firm where it had not made sufficient progress in addressing Audit Inspection Unit (*AIU*) recommendations (described as "Option C" in that consultation document). We believed that such an approach would minimise the potential adverse or unintended consequences.

The Consultation Document refers to events since the previous consultation that have caused the POB to reconsider the issue. We agree that these events have been appropriately characterised by the POB and that in response to those events the proposals have been revised.

We remain concerned about the potential adverse and unintended consequences that may follow from the system of public reporting advocated in the Discussion Paper, and have made some comments below as to how we believe these may be addressed.

The aim of the FRC, to which the POB's own aims and objectives are aligned, is "Confidence in corporate reporting and governance" (Financial Reporting Council Strategic Framework, April

2007). Accordingly, we feel very strongly that public reporting should be done in a manner that does not risk unnecessarily diminishing public confidence in the audit process.

Question 1- Are the processes we intend to follow before high-level reports on individual firms are published appropriate?

The publication of high-level reports on individual firms will increase the information available to audit committees, investors and other stakeholders in assessing their auditors. However, this is an entirely different objective from those which currently direct the reporting of the AIU, specifically (i) enabling the Recognised Accountancy Bodies to exercise their function of the regulation of auditors and (ii) improving the quality of audits of listed and other public interest entities.

As we have said above, such publication carries a risk of unnecessarily diminishing public confidence in the audit process. It is important, therefore, that any public reports provide commentary on the overall assessment of the quality of the audit firm and give a balanced report on the firm's performance of audits, including both the positive aspects of its work and any negative aspects which the inspectors have found. As a result of the current objectives of the AIU, its reports focus on areas where it is felt that improvements can be made, with few comments given on the strengths of a particular firm. Publication of a similar, albeit high level, report would, in our opinion, erode unfairly and unnecessarily confidence in audits. We would support the publication of public reports on individual firms provided that appropriate measures are taken to ensure their balance.

We support the intention to allow firms to provide written comment on the high-level reports before finalisation. It is not clear whether the POB intends that these comments would be published with the high-level report, but we strongly believe that this would be appropriate.

We note the intention to publish completed reports on two or three dates throughout the year. Whilst this may be appropriate on an on-going basis, we would suggest that for the first year, reporting is planned so that as many high-level firm reports as possible, and certainly reports on all those firms subject to full scope inspection visits, are available. This will help avoid undue attention being paid to any single firm or small number of firms whose reports are the first to be released.

Question 2 - Are the processes we intend to follow before new-style reports on individual audits are finalised appropriate?

We consider that there may be benefits in allowing firms to share reports on individual engagement reviews with the relevant client, although we have reservations similar to those expressed above regarding public reports on firms. In particular, we are concerned to see that such reports are balanced.

Our greater concern with respect to these reports is in respect of confidentiality – both the client's and the auditor's – in view of the likely demand for sight of such reports. It is the nature of public companies and other public interest entities that their directors also hold directorships of other entities (in particular, non-executive directors almost always hold board positions on several companies), hence there is an automatic spread of knowledge beyond the audited entity. There will be an interest in the AIU inspection report, and demands for copies, from many parties, including investors, brokers, rating agencies, lenders, anyone performing due diligence, customers and

suppliers. In that context, we believe it unlikely that the reports will remain confidential. In the event of any adverse comment from the AIU, we consider it probable that the likely wide distribution of the report, and wide knowledge of its contents, may cause unnecessary concern as to the quality of the entity's financial statements, as well as to the abilities of the audit firm concerned. This may spark a crisis amongst the entity's stakeholders and the audit firm's clients, and lead to unnecessary damage to confidence in financial reporting and auditing in the UK.

We consider this problem would be exacerbated by the publication of the names of entities whose audits have been reviewed, where another potential risk will arise –there will be speculation which attempts to link comments in the high-level firm report to individual clients. This could be acute where a firm has few clients reviewed, or few clients reviewed in a particular sector.

We do not currently believe that the risks to confidentiality and confidence in companies' affairs can be safeguarded adequately, and believe those risks outweigh any potential benefits of reporting to entities on their individual audits.

Question 3 - Do you have any comments on the Board's proposal that annual reporting on the AIU's work should in future be incorporated in the Oversight Board's annual report to the Secretary of State for Trade and Industry?

We agree that combining the AIU's annual report on its review of audit firms with the POB's overall report to the Secretary of State for Business, Enterprise and Regulatory Reform appears to be a sensible move.

Question 4 - Do you have any comments on the Board's provisional regulatory impact assessment?

The Consultation Document indicates that the additional inspection costs have been estimated at £500,000 (20% of the current total inspection costs), with a similar level of costs being incurred by the firms themselves. It is difficult to know how accurate these estimates are and, in reality, the full costs will only be known once the new regime has been in place for some time.

The Consultation Document states that the costs "are partly within (sic) the hands of the firms themselves and dependent on their approach to report finalisation". Clearly, until each of the first new reports have been drafted by the AIU and shared with the firms, it will not be possible to know how the firms will approach finalisation of the report. It is in the hands of the AIU to prepare balanced and objective reports, which firms will be able to accept with little cost incurred in finalisation.

Conclusion

We support a move towards improved transparency and are supportive of proposals that will help maintain and improve public confidence in the quality of audit attained in our practice and the profession.

An important part of the public reporting process will be a balanced and objective approach to the inspections and the resultant reporting and we look forward to seeing the reports produced on a timely basis and to a sensible schedule.

Deloitte.

We would welcome the opportunity to discuss the proposals and our views further with the POB.

Yours sincerely
for Deloitte & Touche LLP

A handwritten signature in black ink, appearing to read "Gwyn Griffiths". The signature is written in a cursive, flowing style.

Gwyn Griffiths
Partner