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Our Ref: JG/eam  
Your Ref:

Dear Miss Trickett

## **The Professional Oversight Board consultation on 'Reporting on audit quality monitoring'**


We welcome the opportunity to comment on the above consultation paper. Our detailed responses to the questions contained in the consultation document are attached as an Appendix.

We take the issue of audit quality very seriously. In an environment of ever-increasing regulation, keeping pace with developments places continuing demands on our audit specialists. However, we have met these demands in the past and are well placed to continue to meet them in the future. To continue to meet these challenges we must continually review and reassess the way that we operate. It is with that in mind that we have determined our responses to the consultation document.

The AIU has recently concluded our first inspection visit. The review was challenging and intensive. We recognise the need for robust independent review as an important element of maintaining audit quality and public acceptance and understanding of that quality, but we are concerned by the demands placed on the firm by the AIU inspection regime. In particular, whether there is a proper balance between the rigour of review, the impact on the firm and the contribution made to audit quality and public confidence. It is against the background of high costs of inspection that we have considered whether the additional costs associated with public reporting of individual firm's findings can reasonably be borne by those firms

Whilst we acknowledge that this consultation does not invite comment on the AIU inspection regime, we believe it is important to consider that regime when discussing whether or not the reporting process should be changed and reporting on individual firms be introduced. We were concerned at some of the press commentary surrounding the recent publication of the annual report of the AIU on their reviews of Big 4 and other significant firms during 2005/6. In the current environment, where there has been considerable discussion and debate as to whether the concentration of audits of public interest entities by the Big 4 is healthy for UK business, this adverse media reaction is damaging to the mid-tier firms. In order to avoid such media reaction to the public report, it may be necessary for this report to include more balanced discussions of audit quality than is currently the case.





It is clear that anonymity carries a price for firms such as ours. As soon as one firm is revealed as having shortcomings in the public report, then all the firms in that group are potentially viewed as having those shortcomings. The costs of underperformance by any firm in the group, therefore is costly to all firms in each grouping. As such, a regime where firms fail to make progress on remedying any shortcomings damages all. It is therefore easy to see how a 'name and shame' approach is an attractive if you are ahead of the pack and conversely, rather unattractive if you are not, but in the public interest, transparency with regard to not just the auditing profession as a whole, but the individual firms undertaking audits too, is our preferred way forward.

Our views can be summarised as follows:

- improvements to the presentation of the public report are required, with more balanced discussions of audit quality than is currently the case;
- the cost burden of the full public reporting on individual firms is likely to be prohibitive;
- individual reports on firms should be published, but by exception only, if those firms fail to take all necessary steps to address serious issues of poor audit quality within an acceptable timeframe.

We would be happy to discuss our views with you further. If you wish to do this, or require any clarification, please contact Glyn Williams, the firm's national Head of Audit.

Yours faithfully,

**RSM Robson Rhodes.**



## Appendix

### Question 1

**To which of the arguments set out in Part 5, for and against extending public reporting of AIU inspection findings, do you attach most weight and why? Are there other important arguments which we have not captured?**

We consider the strongest arguments for individual reporting are that it affords greater transparency over the inspection findings and avoids the 'guilt by association' issue that is problematic with the group-wide reporting regime. We are also swayed by the argument that individual reporting may assist Audit Committees of certain types of listed entities to identify those firms outside the Big 4 who have a consistent record of performing high quality audits of listed entities.

The arguments against individual reporting are considerable, in our view. We give particular weight to the concerns over the increasing cost burden that will be placed on the mid-tier firms that may already have stretched central resources. We would contend that the scarce resources available to those firms should be directed at those activities that directly impact on audit quality improvements, rather than being expended on protracted negotiations over the details of the reports of regulators.

We believe that reporting on individual firms should be by exception, and that individual reports should only be issued where there are issues of serious quality failures, which the firm in question have not addressed within a reasonable timeframe.

There is no value in producing individual reports on firms highlighting issues of audit quality failures, if those reports are out of date by the time they are issued. If in producing public reports the process becomes overly legalistic, then the lack of timeliness of reporting may well undermine the benefits of public reporting. We believe that the FRC should have regard to the length of the public reporting process in the US, under the PCAOB regime, and takes appropriate steps to ensure that issues of timeliness of public reports does not adversely affect the usefulness of them.

### Question 2


**Which of the options set out at para 6.1 below do you favour, and why? In particular, do you share our view, set out at para 6.2 below, that the nature of weaknesses at a named firm should be disclosed only after the firm, in the opinion of the Oversight Board, has failed to respond positively and promptly to recommendations made to them by the AIU?**

We prefer option D. We believe that the impact on the stability of UK business from a failure in audit quality is such that where any firm has failed to address an issue of serious audit quality failings, they should be publicly held to account. However, it is not a sanction we wish to see imposed for failure to address minor infringements and clear guidelines would need to be developed setting out the precise circumstances in which firms could be sanctioned in this way.

### Question 3

**Do you think that information from AIU inspections on individual audit firms and/or their audits of individual companies should be made available privately to audit committees? If so, what do you think is the most appropriate way of achieving this?**

No, we do not believe that is an appropriate way forward. Audit committees should be entitled to rely on the audit registration process, where issues of audit quality in relation to each of the firms are



considered when determining whether that firm should have its audit license renewed. This in combination with our preferred option, as set out above, should be adequate input to the audit committees' considerations when determining the appointment of auditors.

**Question 4**

**How would you quantify the costs and/or benefits of the options set out at 6.1 below, taking into account Annex A?**

We believe that it is important to consider the costs of implementing some form of individual reporting in the widest context. The Big 4 have considerable central resources at their disposal; the mid-tier firms do not. We are already operating in an environment where there are considerable economies of scale available to the Big 4 firms. To maintain good quality audit manuals, technical support tools, training, appraisal systems etc. takes the same amount of resources if you are a small firm as a large. In the current environment of changes in auditing standards, accounting standards and company law, great care should be taken to ensure that the burden on the central resources in the mid-tier firms is not stretched beyond capacity.

However, the benefits of publicly reporting any serious flaws in audit quality, which are not remedied, are considerable. The reliability of audit quality in respect of the entities, whose audits fall under the remit of the AIU, is important to the economy as a whole. We consider therefore that, on balance, the financial community should be made aware of those firms who do not take appropriate steps to address serious audit quality failings within a reasonable timeframe.

