

From the Chief Executive **Allen Blewitt**



Julian Rose
Financial Reporting Council
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04 August 2006

Dear Mr Rose,

I write to provide ACCA's views on the issues addressed in the Discussion Paper *Choice in the UK Audit Market*. ACCA is the largest and fastest-growing international accountancy body with 260,000 students and 110,000 members in 170 countries. Many of our members are partners in, or staff of, the transnational audit firms that are active providers of audit services to large listed companies; many are involved in the financial reporting and corporate governance functions of large companies and most would share the view that the healthy functioning of markets is of paramount importance.

It is important to recognise the strong and excellent work undertaken by UK auditors. We do not feel that the Discussion Paper itself promotes confidence in the competitive UK audit market. It is a key test that any changes proposed as a result of this consultation should not diminish the market's existing effectiveness nor the quality of auditing.

The Paper perpetuates the divide between the 'Big Four' audit firms and others which contributes to the perception that some are second class citizens. While there may be significant differences in firm's capacities to act for the very largest global companies, the same regulations and rigorous standards apply to all. The publication of the 2005/6 AIU report confirmed that both groups of firms had, in their view, generally conducted audits to a high or acceptable standard.

We agree with the observation in the Paper that the characteristics of the UK audit market are shared with other markets worldwide. Similarly, any solutions proposed are unlikely to be successful unless they make sense in a global context.

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The Discussion Paper poses several questions and we answer these in the Appendix to this letter, insofar as they are relevant to our viewpoint as an accountancy body.

If you have any questions on our response please direct them in the first instance to David York, Head of Auditing Practice.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Allen Blewitt', is written over a light blue horizontal line.

Allen Blewitt

Section 1.01 Appendix

Q1 Do you agree that the focus of the debate should be on the degree of choice in the market for audit services to large public companies, rather than other features of this market?

Q2 What do you regard as the most important criteria for evaluating any opportunities for mitigating risks arising from the level of choice in the audit market?

The Paper indicates that the degree of choice could have adverse consequences in terms of audit quality and price. We agree that price is not actually an important issue and that the focus should be on audit quality. The Oxera study did not address audit quality directly but we are aware of strong views expressed by commentators that one reason that companies have not changed auditors frequently is that they are satisfied with the quality of auditing. We are of the view that audit quality is itself only an important issue where the availability of any audit services is a problem, that is where there is no firm that can meet a particular client's needs. Difficulty could arise through the withdrawal of a major firm from the audit market (which we comment on further below) or a change to an unsuitable auditor prompted by some other event.

The Oxera report's findings regarding the views of audit committee chairs were in relation to a broad statement '*Currently, there is enough choice of alternative auditors in the market for my company to choose from*'. Twice as many agreed as disagreed and narrative in the report indicated that any problem of insufficient choice was manifest only in the very largest companies.

Given the remote chance of a catastrophic event and the restricted number of very large companies affected, we are drawn to the conclusion that one-off measures by the regulator at the time are likely to be the most cost effective solution to any problem. Earlier, market-wide solutions would inevitably entail substantial costs that would fall disproportionately on smaller listed companies.

Q3 / Q4 / Q5 - Relating to greater market participation by non-Big Four firms.

We do not believe that greater market participation by non-Big Four firms would address the danger of disruption to the audit of the largest listed companies for which auditor choice is perceived as a problem. This is not to say that greater participation is not a good thing for the market as a whole; it may both increase choice and add competitive pressure. Inevitably, any change to the status quo will be in response to a combination of pressures, but key factors are the desire of firms to enter the market and the attitude of those who appoint them. While the Oxera report and the processes that follow undoubtedly contribute to these

pressures, we see no role for regulatory action that would distort what is, at present, a competitive and successful market.

Q6 We invite views on steps that could be taken to mitigate the risk of unnecessary withdrawal of a firm from the market . . .

Q7 We invite views on steps that could be taken to mitigate the effects of a voluntary or involuntary withdrawal of a firm from the audit market . . .

The Paper cites circumstances where leaving the market is precipitated by damage to reputation prior to the full circumstances of a problem being known. Clients deserted Arthur Andersen as it was indicted for obstructing justice by shredding documents related to its audit of Enron. We believe that lessons have been learned by many parties and a similar event it is a remote possibility. There have been more recent corporate scandals and indeed more recent legal actions (albeit relating to fraudulent tax shelters) that have not had such significant global consequences.

Solutions may be proposed that are disproportionate to the risk of a major firm leaving the market and we caution against justifying their adoption in this context. For example, a joint auditor requirement, such as operates in France, would be one way to provide continuity should a major firm leave the market. Such a solution would, however, be in our view wholly inappropriate given the size of the UK market and the inefficiencies and market distortion inherent in such arrangements¹.

It is inevitable that if a major auditing firm left the market suddenly, that firm's personnel and that firm's clients would remain. ACCA would take appropriate steps to protect the interests of affected members and students. For example, whilst qualified staff are able to transfer to another employer without restrictions, trainees with a particular firm may be more vulnerable as they may suffer disruption to their studies and have difficulties in transferring their training contracts. Audit firms and professional bodies should be encouraged to consider what contingency plans could be put in place to enable trainees to continue their studies without interruption in the short-term.

¹ FRC may wish to refer to the draft paper 'What are the Determinants of Normal and Abnormal Audit Fees in France?', *Sophie Audousset – Coulier*, presented at the 29th Annual Congress of the European Accounting Association, Dublin, March 2006.