



Ms Susan Currie
Financial Reporting Council
8th Floor
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28 August 2015

Audit firm governance code: review of implementation and operation

Dear Ms Currie,

PricewaterhouseCoopers LLP welcomes the opportunity to comment on the Financial Reporting Council's (FRC's) proposals for revising the 2010 version of the Audit Firm Governance Code (the Code).

In this letter we have set out the principal themes of our response and in the attached Appendix 1, we set out answers to the detailed questions asked in the FRC's consultation paper. In Appendix 2, we present views from our independent non-executives to supplement the messages in our response.

A framework for defining the public interest

1. The concept of the public interest is at the very heart of the Code. In discussing the fundamental purpose of the Code, the FRC rightly begins by considering the public interest. However, in the consultation paper, the FRC has stopped short of defining the public interest, other than emphasising the importance of audit quality in this regard.
2. We believe that the profession and the FRC should work together to create a framework through which we can share a common understanding of the public interest. We suggest that this framework should identify the many different stakeholders who have an interest in the capital markets system. Some (e.g., equity shareholders) will have a direct financial interest. Others (e.g., our local communities) have a less direct, but nonetheless important, economic interest.
3. Once we agree on this framework and these stakeholders, we can discuss constructively appropriate engagement approaches, and we can state with confidence that we "take account of the public interest in our decision making". We believe that the result will be closely aligned to our current articulation of who we are, which includes to "Do the right thing for our clients, our people and our communities".
4. The identification of these different groups of stakeholders will also illustrate that it may not always be possible to "act in the public interest" as, in some cases, the interests of different groups of stakeholders may conflict. Our responsibility should be to take account of the many facets of the public interest as we make decisions. Importantly, we should take account of the interests of shareholders in listed companies alongside the interests of other stakeholders.

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The purpose of the Code

5. The fundamental purpose of the Code is currently unclear, as evidenced by the debate surrounding this consultation. We support a much simpler, clearer articulation of the purpose which begins with the consideration of the public interest. We suggest that the purpose of the Code should be to ensure that audit firm governance is designed to take account of the public interest through:
 - a. the promotion of audit quality;
 - b. monitoring of other activities carried out by an audit firm, to ensure that conduct is appropriate and does not create undue risk to the audit firm; and
 - c. setting expectations for high standards of governance over the whole firm.
6. In referring to the public interest at the outset, we are of course mindful of our recommendation to develop a framework which facilitates a common understanding of the public interest.
7. This expression of purpose is broadly consistent with that set out in paragraphs 16 - 18 of the consultation; we believe that there will be a benefit in articulating the purpose of the Code in as concise and simple a form as possible.
8. In paragraph 16 of the consultation, the proposed purpose of the Code is set out as “the promotion of high quality statutory audit in the interests of shareholders” (emphasis added). We believe that the benefits of the Code should not be restricted to statutory audits alone, nor only to shareholders in listed companies, but should extend to the provision of assurance to the wider stakeholder community, many of whom have much at stake if trust is not maintained. If the duty of care in respect of statutory audit was to be extended to all stakeholders, rather than the existing remit where the duty is to shareholders, then of course, the debate regarding the unlimited liability faced by auditors will need to be progressed.
9. In the same paragraph of the consultation, we welcome the FRC’s recognition that high quality audits are not solely a product of compliance with laws, regulations and standards. Our view is that “good” audits are those which promote trust in the system, through increasing confidence in audited financial statements.

Accountability of the independent non-executives

10. The Code currently states that the Independent Non-Executives (INEs) have a duty of care to the firm. We concur with this and we question the proposal that there could be additional accountability to the public, or to regulators. This would be confusing and could lead to unresolvable conflicts; formalising accountability to the regulator could also lead to an expectation that the regulator is somehow “responsible” for the quality of governance in firms.
11. PwC INEs operate in an advisory capacity and are not decision makers within the business (although their advice is often highly influential). Our INEs seek to influence the partnership’s decision makers, but they are not the final arbiters when it comes to choosing a course of action. As a consequence, it would be inappropriate to hold them accountable for the partnership’s actions.



Engagement with stakeholders

12. Section F.1 of the current Code suggests that audit firms should have a dialogue with their stakeholders (including shareholders, audit committee members and others) about matters relevant to the Code. We believe that this dialogue is critical to the success of the Code, as well as to our ability to take account of the public interest, as explained above. However, in our experience, there is limited enthusiasm for engagement from within the corporate and investment communities, aside from the “corporate governance” specialists in investment institutions. We would welcome opportunities to engage more broadly and we support the FRC’s work to promote this engagement through the Stewardship Code and other activities.
13. We are committed to transparency about our compliance with the Code and the activities of our INEs. Currently, we report on these areas in our Transparency Report. We would welcome any support from the FRC to promote these disclosures further; we hope that further attention to these areas would prompt more engagement of the type mentioned above.

Governance structures

14. The consultation considers whether specific governance structures should be applied to the audit business of audit firms. We do not believe that such specific governance structures are necessary. In fact, we consider that such structures could be detrimental to audit quality through introducing an artificial separation between the regulated and unregulated parts of the business. Currently, both parts of our business are held to the same high ethical standards. This is not only good practice, but also ensures that when staff from the non-regulated part of the business are engaged in audit work (for instance tax specialists working on an audit), they share the same ethical commitment as our audit staff.
15. As we have previously discussed, the model of multi-disciplinary audit firms is critical to the maintenance of audit quality and we do not support any move which seeks to impose artificial separation within the multi-disciplinary structure.
16. In addition, imposition of specificity in governance structures would be contrary to the spirit of the Code, which allows individual design of governance structures to reflect individual firm structures and circumstances.
17. We suggest that further focus on audit quality could be introduced into the agendas of the existing governance bodies of firms.
18. As we have previously discussed with you, we have found adoption of the Code, and in particular the independent insight and challenge brought by our INEs, to be beneficial. We have already shared our views and experiences with other PwC network firms who will take them into account as their own governance structures evolve. We do not believe it would be appropriate for the FRC to seek to impose specific governance recommendations outside of the UK; in fact we believe it would be unworkable. Such a move would be extra-territorial and, more importantly, might not



take account of national legal, regulatory and cultural differences.

‘Comply or explain’ governance and the UK Corporate Governance Code

19. The UK Corporate Governance Code was designed to respond to the separation of ownership and management interests inherent in most corporate structures. The FRC recognises in the Code that most audit firms are structured as partnerships (albeit often limited liability partnerships); this means that some care is needed when using the UK Corporate Governance Code as a reference point for the Code.
20. Elements of the UK Corporate Governance Code which could merit further consideration in the context of an audit firm, and indeed some of which PwC has already adopted, include:
 - a. the new risk management recommendations introduced in the 2014 Code;
 - b. greater consideration of diversity; and
 - c. term limits on INE’s appointment.
21. The structures of audit firms do not allow for the same committee structure as contemplated by the UK Corporate Governance Code. However, we would expect the independent non-executives, in fulfillment of their responsibilities, to have a role in discussing key appointment and remuneration policy decisions with executive management.
22. We do not support any moves to involve investors or regulators in INE appointment decisions. As noted in paragraph 11 above, the INEs operate in an advisory capacity, and firms should have an unfettered ability to select their advisors according to their identified needs.
23. We further note that the success of the UK Corporate Governance Code is at least partly due to the ‘comply or explain’ principle that underpins it; this same principle underpins the Code. There are a number of the elements of the consultation which suggest a move towards a more prescriptive approach; we strongly support maintenance of the ‘comply or explain’ principle. It encourages governance approaches which are properly tailored to individual firms’ circumstances and, further, prompts debate and challenge with external stakeholders. The best kind of soft law is measured by its balance: it should be effective but non-constraining and additions should be evaluated based on bringing clear benefits.



Further details on all of these points can be found in the appendices. Gilly Lord, Head of Regulation and I would be delighted to discuss our response with you if that would be helpful.

Yours sincerely

A handwritten signature in black ink that reads 'Ian Powell'.

Ian Powell
Chairman and Senior Partner

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No	Question	Response
A	<p>We welcome views on the above expression of the public interest in this context [ie firm's responsibility and INE's role] and whether it should be put into the Code. (para 19)</p>	<p>A framework for defining the public interest - We agree that the meaning of the public interest, in the context of a firm's responsibility, and the INE's role within that, is not clear in the Audit Firm Governance Code (Code/AFGC) and we agree that a legalistic approach to defining it would not be helpful. However, we believe it is important that some level of guidance should be incorporated into the new Code around the concept of the public interest and also that the expression of the term within the Code should not be drawn too narrowly around audit quality alone.</p> <p>The FRC acknowledges, in paragraph 19, that the question of public interest is being discussed in other fora, notably by the ICAEW which may soon issue guidance on this area to enhance the clarity of its Code of Ethics. Any amendment to the Code in this area should align with the ICAEW's guidance on the public interest; lack of alignment could create confusion. We suggest that the FRC should work with the profession to develop a framework through which we can share a common understanding of the public interest. We suggest that this framework should identify the many different stakeholders who have an interest in the capital markets system. Some (e.g., equity shareholders) will have a direct financial interest. Others (e.g., our local communities) have a less direct, but nonetheless important, economic interest. Once there is agreement on this framework and these stakeholders, we can discuss constructively appropriate engagement approaches. The identification of these different groups of stakeholders will also illustrate that it may not always be possible to "act in the public interest" as, in some cases, the interests of different groups of stakeholders may conflict. Our responsibility should be to take account of the many facets of the public interest as we make decisions.</p> <p>The firm's responsibility</p> <p>Once a framework for defining the public interest has been agreed, we then need to agree the level of an audit firm's responsibility. An important detail is that our public interest responsibility can have different interpretations based on the language used: e.g., whether one "<u>acts in the public interest</u>", "<u>takes account of the public interest</u>", or "<u>takes the public interest into consideration</u>". These could each result in different expectations of our level of responsibility.</p> <p>The Appendix to the Code which sets out the involvement of the INEs, says INEs are: "a witness to a firm's <u>commitment to the public interest</u>". Elsewhere, the Appendix refers to the firm's culture being committed to '<u>working in the public interest</u>', whilst the Code consistently expects the firm to take the public interest <u>into consideration</u> in its decisions.</p> <p>In the introductory section to the Code, the firm's responsibility is described using a number of different phrases including "acting in a way that properly takes the public interest <u>into consideration</u>" and "demonstrate their <u>commitment to good governance and the public interest</u>".</p>

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		<p>We believe that the most appropriate and consistent reference should be “taking account of the public interest” as these words best reflect the need to balance the needs of different stakeholders.</p> <p>The INEs’ role Paragraph 34 suggests that the INEs’ role should be defined on the basis of “promoting the public interest”. Since the meaning of the public interest is not yet clear, we do not agree that this is the best way to define the INEs’ role. We suggest that instead that the INEs’ role should be aligned to the purpose of the Code, as explained in our covering letter and in our answer to question 2 below.</p> <p>Public interest and commercial interest of firms – In paragraph 67 of the consultation document, the drafting implies that the FRC’s Ethical Standards require the public interest to supersede all commercial interests of the firm. Our understanding is that the Ethical Standards require that firms ensure a control environment that places adherence to ethical principles and compliance with Ethical Standards above commercial considerations. The ICAEW’s Code of Ethics states that individual accountants must <i>take into consideration</i> the public interest. Even taking these two together does not imply that the public interest must at all times supersede commercial interests.</p>
B	<p><i>We are keen to seek views on the extent to which the Code has achieved its stated purpose and delivered the above hoped-for benefits. (para 30)</i></p>	<p>Purpose of the Code - The purpose, as articulated in the 2010 Code, is multi-dimensional and a little complex. The primary purpose is stated as: to provide a formal benchmark of good governance practice, against which firms which audit listed companies can report for the benefit of shareholders in such companies. Subsequently, there follows a list of ‘intended benefits’/‘roles’ of the Code, which are summarised and referred to as ‘objectives’ in the FRC’s consultation: improving firms’ governance; increasing competition and choice in the market and reducing risk of an exit of a firm from market; enhancing firms’ reporting and stature as good practice governance exemplars.</p> <p>We suggest that in revising the Code, the FRC makes a simpler, and clearer, expression of the Code’s purpose.</p> <p>In terms of achieving the hoped-for benefits, we have the following observations:</p> <ul style="list-style-type: none"> • In PwC’s experience, our governance has been enhanced by the establishment of our Public Interest Body (PIB) and the challenge that our INEs bring to management’s decision making. • A small number of listed company shareholder representatives have shown increasing interest in the quality of governance in major audit firms. However, our experience is that this level of interest is not common, particularly outside of the corporate governance community. We would welcome further opportunities to engage with a wider group of investors. Promotion and monitoring of the FRC’s Stewardship Code could be one way of encouraging this engagement. If we achieve constructive

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		<p>dialogue between all participants in the capital markets, we are more likely to achieve safe capital markets for all.</p> <ul style="list-style-type: none"> • It is hard to establish a link between the Code and increasing choice and competition in the market and we are sceptical about the value of including this as an aim of the Code. The market is, and continues to be, highly competitive. Recent regulatory developments have promoted more activity in audit tendering and companies are changing their auditors more frequently as a result. Changes of auditor will also be required for public interest entities when the EU mandatory audit firm rotation rules are implemented in the UK. One area where there is more opportunity to promote competition on the basis of audit quality is in the use of Transparency Reports. These important documents include information about audit firm governance and the systems and controls in place to maintain audit quality. We would like to see audit committees and investors make more use of these documents when assessing audit quality and we suggest that the FRC could do even more to promote and publicise these documents. • We would expect to include a section on compliance with the Code in our Transparency Report. Therefore we do not believe that further prescription on reporting of Code compliance is necessary; firms have the opportunity to be innovative in their reporting on governance and use this as a competitive tool. We agree with the FRC’s stated reluctance to turn the Code into a “comply” rather than “comply or explain” document. • One consequence of improved governance could be a lower risk of a firm exiting the market as a result of a catastrophic failure in its business model. However, such an event would usually be the consequence of a complex series of factors, which would probably include governance failings alongside a number of other of events. We do not, therefore, believe that it is valid to include “helping to reduce the risk of a firm exiting the market” as an intended benefit of the Code.
C	<p><i>Even if formal accountability (of INEs) outside the firm is not possible we believe boards, public interest committees and INEs should regard themselves as being accountable to the public and conduct themselves accordingly. That means ensuring there is high quality public transparency of their role and work so that they can be</i></p>	<p>As we set out in our answer to “A” above, we believe that it is important that we collaborate to develop a framework through which we can share a common understanding of the public interest. This work is essential if boards, public interest committees and INEs are to have an explicit responsibility directed towards the public with an expectation of their conduct as a consequence.</p> <p>Again, as we explain in “A”, the language used to express this responsibility is important. We do not believe, for example, that it is possible for INEs to have a duty of care to the firm <u>and</u> to regard themselves as formally accountable to the public. There could easily be cases where these two situations create irresolvable conflicts. However, it would be perfectly reasonable to ask INEs, boards and public interest committees to take account of the public interest as they fulfil their duty of care to the firm. This may, of course, require</p>

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	<p><i>questioned and challenged and that if there is evidence of public disquiet they should respond to this. We welcome views on this. (para 35)</i></p>	<p>those charged with governance to make difficult judgements as they weigh up the differing interests of stakeholder groups, but we regard this as an appropriate component of their governance responsibilities.</p> <p>We also accept that there may be situations where INEs are called upon to give a public account of how they have discharged their responsibilities. However, in this sense, we believe that many INEs already consider themselves ‘accountable to the court of public opinion’ whether formally driven by a Code, or otherwise.</p> <p>The onerous nature of the accountability as expressed in the consultation document could even act as a deterrent to recruiting high quality INEs who could anticipate spending a large proportion of their time dealing with challenges from members of the public who may have specialist interests. This could jeopardise the time spent in oversight of the audit firm and its management.</p>
1	<p><i>Firstly, and most importantly, is the stated purpose of the Code still valid? (para 55)</i></p>	<p>In answering this question we also refer to the comments we have made in Sections A and B above.</p> <p>In addition, we note that there is an important decision to be made by the FRC about whether the Code should seek to benefit equity shareholders alone, or a wider stakeholder group. If the latter, this should be made clear and consistent throughout, although we believe that the aspects of the Code relating to interaction between the firms and investors in listed companies should be retained and emphasised.</p>
2	<p><i>Do you agree that the Code’s purpose should be redefined in this way? (para 59)</i></p>	<p>In answering this question we also refer to the comments we have made in Sections A and B above.</p> <p>We agree with the aim of simplifying the purpose of the Code and suggest that it could be expressed as follows:</p> <p><i>“To ensure that audit firm governance is designed to take account of the public interest through:</i></p> <ul style="list-style-type: none"> <i>a. the promotion of audit quality;</i> <i>b. monitoring of other activities carried out by audit firms, to ensure that conduct is appropriate and does not create undue risk to the audit firm; and</i> <i>c. setting expectations for high standards of governance over the whole firm.”</i> <p>The FRC suggests in paragraph 58 that the purpose should be redefined to introduce a clearer context for the public interest which is to (1) focus on audit quality; (2) focus on the firm’s reputation more broadly including oversight of non-audit businesses; and (3) focus on prevention of firm failure. Our suggested purpose incorporates the first and second of these, and makes it clear that audit firms should take account of the public interest, rather than being held accountable for always acting in the public interest – as we explain above, we believe that such accountability could lead to irresolvable conflicts.</p>

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		<p>We do not agree with the FRC's third proposal that the Code should focus on prevention of firm failure. Successful implementation of the Code could play a part in mitigating the risk that audit firms will fail, but we do not believe that it is realistic to suggest that the Code itself will prevent firm failure.</p> <p>We agree that the existing Code is unclear on the meaning of "public interest" and, as suggested in A, we would encourage the FRC to collaborate with the profession in developing a framework for the common understanding of the public interest.</p> <p>We also suggest elements of the Code's current objectives should be removed. For example, the Code includes an objective of "enhancing competition and choice in the market". The FRC has acknowledged in its consultation (paragraphs 43-45) that the Code has had limited success in that area and that the CMA has introduced provisions to facilitate enhanced competition, rendering any additional provisions in the Code redundant.</p> <p>Paragraph 16 includes a definition of "a quality audit" as one which provides a high level of assurance. It is unclear how one would measure whether the level of assurance was high or low; it needs to be the right level to support the audit opinion. There is no agreed definition of audit quality that currently exists, although the guide issued by the FRC to audit committees on assessing audit effectiveness is helpful, as is the work done by the larger firms in seeking to communicate key indicators of audit quality.</p> <p>Paragraph 16 also introduces the concept of "the societal value of audit". If this term is to be retained, we suggest that it should be defined more clearly.</p> <p>In paragraph 20, the FRC suggests that in considering wording on the public interest, which may potentially be incorporated into the Code, it should be recognised that "the spirit with which the public interest is pursued is as important as the definition." We suggest that the reference to the "spirit with which the public interest is pursued" is unhelpful language to consider introducing into the Code, since it lacks clarity. As we discuss earlier, the profession and the FRC first need to work together to develop a framework for a common understanding of the public interest before we can make these type of statements.</p>
3	<p><i>Should there be separate governance arrangements for audit? What might such arrangements look like? (para 65)</i></p>	<p>Oversight of audit quality - We fully support the FRC in its objective of establishing strong oversight of audit quality. We do not believe that this will be best achieved by introducing separate governance arrangements for audit and we have observed evidence that the existing approach is working well.</p> <p>In our firm, improvements in audit quality inspection results since the implementation of the Code suggest that oversight of audit quality by our Public Interest Body is already achieving successful results. Within our current model the PIB receives detailed information from the Executive Board enabling review and</p>

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		<p>constructive challenge of the systems and processes in place to maintain and improve audit quality. In addition, the PIB Chairman participates in annual meetings with the FRC’s Audit Quality Review Team and each of the INEs takes a close interest in the audit quality inspection process and findings each year</p> <p>Separate governance arrangements for audit would create the perception of “ring-fencing of the audit practice”. We do not support this direction of travel. We work hard to instil a consistent ‘One Firm’ culture throughout our firm. Creation of separate governance arrangements for audit oversight would undermine this single culture. All of our professionals must comply with the core elements of the ICAEW Code of Ethics and with our own PwC Code of Conduct [http://www.pwc.com/gx/en/ethics-business-conduct/pdf/pwc-global-code-of-conduct-update.pdf]. Many professionals in the non-assurance lines of service contribute their specialist skills to audits, and so it is important that their sense of responsibility to follow the same ethical responsibilities as auditors is maintained.</p> <p>Ultimately, ring-fencing of the audit practice would undermine the ability of audit firms to maintain multi-disciplinary practices which, in our view, are key contributors to sustaining high audit quality. Multi-disciplinary practices enable us to attract high calibre recruits who are looking for broad experience in their work. This broad experience, of course, contributes to their business understanding, which is an essential component of high quality audits.</p> <p>In addition, the imposition of specificity in governance structures would be contrary to the spirit of the Code, which allows individual design of governance structures to reflect individual firm structures and circumstances.</p>
4	<p><i>Should the Code include more detail and impose more requirements on tone at the top and professionalism more generally? (para 68)</i></p>	<p>Tone at the top - We strongly support a culture of ethics and professionalism and an appropriate tone at the top and note that this is reflected in the FRC’s Ethical Standards. It is also reflected in the ICAEW’s Code of Ethics, applicable to all partners and staff in the audit firms who are members of the ICAEW. Because of this existing regulatory base, we do not see a need for further emphasis in the Code. In fact, such an approach could detract from the personal responsibility that members of ICAEW have under the ICAEW Code of Ethics.</p> <p>In addition, culture is an area difficult to prescribe or define in regulations and codes. An overly detailed approach in the Code could devalue the principles on which the Code is based.</p> <p>A number of the large audit firms already disclose information about their tone at the top and culture in their Transparency Reports (see PwC examples at p7 “Our people and culture” and p38 “Culture and tone at the top” of our 2014 Transparency Report). These disclosures provide the starting point for investors and regulators to understand and challenge culture in audit firms. As we point out in our answer to Question A, we would support the FRC in promoting more use of these important documents.</p>

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5	<p><i>Do you agree that the concept of the Code should be spread elsewhere in the world? How might this be achieved? (para 70)</i></p>	<p>In the introductory section of the Code, it is suggested that it may make sense to look beyond the national firm in considering application of Code principles and compliance with the Code provisions. In the executive summary section of the consultation, it is suggested that the principle of external challenge could be adopted internationally. Constitutionally this would be very difficult, if not impossible, to impose. We do not believe it would be appropriate for the FRC to impose specific governance recommendations outside the UK; such a move would be extra-territorial and more importantly, might not take account of national legal, regulatory and cultural differences.</p> <p>From our UK firm's perspective, we have found compliance with the Code to be very beneficial. We are already sharing aspects of our experience with other firms in the PwC network which are considering an evolution of their own governance structures, tailoring good practices to reflect their local culture.</p> <p>The introductory section of the Code also suggests that disclosures might more usefully refer to the firm's international network. Such disclosures are already made in PwC's Transparency Report (please refer to Section 2) although we would be happy to consider amending or enhancing this disclosure in response to specific suggestions.</p> <p>In future consultations, and in any iteration of the Code, it would be helpful if the FRC could clarify references to "network entities" and "network organisations". These terms are used interchangeably in this consultation paper, but could have different meanings, depending on the way in which firms are organised.</p>
6	<p><i>How might the independence of INEs be protected and demonstrated? (para 80)</i></p>	<p>The independence of INEs is taken extremely seriously as noted by the FRC in its consultation. We believe that there is no need to amend existing arrangements for protecting and demonstrating the independence of INEs.</p> <p>Situations not addressed by the Code – In paragraph 77 of the consultation, two examples are cited as situations where the Code may need to address specific problems. One of these examples is a clear breach of the independence principles set out in the Code; the other relates to our firm. The example which relates to PwC concerns a situation which arose where our audit practice was tendering for the audit of a client where one of our INEs was a director. We took the guidance in the Code into consideration before we acted and we then took immediate steps to ensure that independence was not compromised. Neither of these examples therefore make a case for the Code to include exceptional circumstances, since both are catered for already. Whilst the Code <i>could</i> be amended to include the two examples cited, we strongly believe that it would be less effective to add multiple examples, rather than to ensure that the high level principles are emphasised.</p> <p>We note that in the situation involving PwC, we ensured that there was full transparency of the situation through disclosure in our Transparency Report. Detailed disclosure in Transparency Reports can be effective in demonstrating INEs' independence and can provide regulators and investors with an opportunity to assess</p>

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		whether the Code’s principles have been followed, and where this isn’t the case, that there are adequate explanations for a different approach.
7	<i>Should the firms follow a standard process in appointing INEs, including all such positions being publicly advertised? (para 80)</i>	We do not believe that there is a need for a standard process, including public advertisement, to be followed in the appointment of INEs. Such a process would result in many applications of which most would probably fail the independence test. This would be time consuming and inefficient for all concerned.
8	<i>What engagement, if any, should investors in audited entities have into an audit firm’s appointment of INEs? (para 80)</i>	<p>Our experience is that Investor engagement with audit firms is inconsistent and usually carried out only by a vocal minority of investors who may not have views representative of the wider investor community. We do not believe, therefore, that it would be appropriate for there to be consultation with investors on INE appointments; in fact such an arrangement could lead to sub-optimal outcomes. We note also that there are practical challenges for both firms and investors in terms of engagement activity, and given time constraints on both sides, we believe that more benefit could be gained through other types of engagement.</p> <p>We agree that appointment of INEs could be an appropriate topic for discussion in stakeholder meetings although we anticipate that this discussion would be informal rather than constituting formal consultation.</p>
9	<i>Should the FRC or any other regulator have a role in the appointment of INEs; perhaps a right of veto? (para 80)</i>	As noted in our response to question 8, we agree that the appointment of INEs could be discussed in stakeholder meetings. Such a discussion would promote transparency over the appointment process and decisions. We do not believe however, that there is any compelling argument for the FRC, or any other regulator, to have a more formal role in the appointment of INEs .
10	<p><i>Which of these [aspects of CG Code listed below], if any, should be incorporated into the Code? Are there any other aspects of the Corporate Governance Code which should also be considered? (para 82)</i></p> <ul style="list-style-type: none"> <i>The inclusion in firms’ transparency reports of a viability statement providing an assessment of long term solvency and liquidity</i> 	<p>In considering our answer to this question, we were mindful of the significant differences that exist between an audit firm which is a limited liability partnership and a limited company with external shareholders. The “separation” issues that the UK Corporate Governance Code is seeking to address (i.e., separation of owners and managers) compared to those experienced in audit firms (limited separation of owners and managers, but separation of both of these parties from the “public interest”) are quite different. For the most part, these differences should give rise to different responses. This means that we believe that any “default” application of the UK Corporate Governance Code principles to audit firms would be inappropriate.</p> <p>Notwithstanding this overall comment, we agree that there could be some aspects of the UK Corporate Governance Code which would be beneficial if introduced into the Code. We have commented on each of the FRC’s suggested additions below:</p> <p>Requirement for INEs to have ‘recent and relevant financial experience’ – We don’t believe that this requirement is necessary for an INE in an audit firm. The requirement for at least one member of a listed company’s Audit Committee to have “recent and relevant financial experience” is a consequence of the Audit Committee’s responsibility for the integrity of the financial statements and overseeing the audit of those</p>

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	<ul style="list-style-type: none"> • <i>Term limits on INEs' appointment</i> • <i>Transparency around the remuneration of INEs</i> • <i>A minimum number of INEs per firm</i> • <i>A requirement for at least one INE to have recent and relevant financial experience</i> • <i>An independent Chairman</i> • <i>Greater consideration of diversity</i> • <i>A formal role for INEs on remuneration, nomination, risk and/or audit committees</i> 	<p>financial statements. The INEs in an audit firm do not have any equivalent responsibilities. At PwC, these responsibilities would fall to our Audit Committee.</p> <p>Viability statement – We would not object to making such a statement in our Transparency Report, although we would question the value of the disclosure. The biggest risk to the viability of an audit firm is a severe blow to our reputation which could result from litigation, although also from other causes. Any statement of viability would, therefore, need to assume that no such event would occur; other assumptions would be of much less materiality.</p> <p>Term limits on INEs' appointment - At PwC we have already introduced term limits on INEs appointment, which are staggered so as to allow for flexibility and to avoid all INEs standing down at the same time.</p> <p>Independent Chairman - At PwC, the chairman of our public interest body is independent, however we recognise that the different structures adopted by other firms may not easily allow the appointment of an independent chairman. We continue to support a Code philosophy that allows flexibility for firms to adapt governance structures to their own unique characteristics.</p> <p>INEs on remuneration, nomination, risk and/or audit committees – At present, each audit firm has the flexibility to design governance structures which are tailored to their own unique characteristics; there is no requirement for the establishment of remuneration, nomination, risk and/or audit committees, unlike in the world of listed corporates. We therefore believe that it would be illogical for the Code to require a formal role for INEs on these committees, since in some audit firms the committees do not exist. In the structure PwC has adopted, the INEs have control over the agenda for meetings of the Public Interest Body. This means that they can exercise their own judgement as to the areas they wish to oversee, which could include any of the items listed above.</p>
11	<p><i>To whom should the boards, INEs and public interest committees be accountable? How should this accountability be discharged, including to the FRC? (para 88)</i></p>	<p>In answering this question we refer also to our comments in Section C, above.</p> <p>INEs duty of care - The 2010 Code is clear that the INEs' duty of care is to the firm. Principle C2 states that they should command the respect of the firm's owners and collectively enhance shareholder confidence by virtue of their independence, number, stature, experience and expertise. We believe that this principle should be maintained and that supporting statements should emphasise rather than confuse this principle.</p> <p>Principle C1 of the 2010 Code further explains this duty of care by noting that INEs' involvement should "collectively enhance shareholder confidence in the public interest aspects of the firm's decision making, stakeholder dialogue and management of reputation risks, including those in the firm's business that are not otherwise effectively addressed by regulation." In our opinion, the INEs should remain accountable to the audit firm, and only to the audit firm, whilst they continue to ensure that the firm's decision making takes account of the public interest.</p>

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		<p>We do not believe, for example, that it is possible for INEs to have a duty of care to the firm <u>and</u> to regard themselves as formally accountable to the public. There could easily be cases where these two situations create irresolvable conflicts. However, it would be perfectly reasonable to ask INEs, boards and public interest committees to take account of the public interest as they fulfil their duty of care to the firm.</p> <p>Shareholders, regulators and other stakeholders should observe this exercise of responsibility as they engage with audit firms, and through the public reporting that appears in firms' Transparency Reports.</p> <p>We don't agree with the proposal in paragraph 88 that a viability statement in a firm's Transparency Report could be made jointly by management and INEs. INEs should not be jointly responsible for any new statements mandated for firms' annual or transparency reports; they are not part of a unitary board of directors responsible for the truth and fairness of a firm's financial and narrative reporting.</p>
12	<i>Should the Code include specific provisions on the firms' Boards and Public Interest bodies engaging with and disclosing certain matters to regulators? (para 88)</i>	As noted in paragraph 84, the current system for engagement between INEs and regulators appears to work well. The FRC meets directly with the PwC INEs and there is constructive dialogue. We do not believe there is a need for additional disclosure to be prescribed.
13	<i>Is greater transparency sufficient? What else can be done? (para 88)</i>	<p>Transparency of INEs' activities - The FRC's proposals include either incorporating into the Transparency Report, or via a separate letter to the FRC which would be published, the INEs report on their activities to discharge their public interest responsibilities. In the case of PwC UK, the PIB Chairman already makes an annual report giving an account of the PIB's activities which is included in the PwC UK Transparency Report and we assume that therefore we would already meet any new requirement of this nature.</p> <p>A fair, balanced and understandable statement – the FRC's consultation document also suggests that a "fair, balanced and understandable" statement could be made by a firm's management in respect of aspects of an audit firm's reporting. We would suggest that it would be most appropriate to make a "fair, balanced and understandable" statement in respect of the Annual Report of an audit firm; to attach the statement to the Transparency Report in isolation would capture only one (albeit important) aspect of a firm's reporting.</p>
14	<i>Should the Code be applied to a wider group of firms? (para 90)</i>	We do not believe there should be a requirement for smaller audit firms to report under the AFGC, but given that one such firm has chosen to do so, market forces and competitive edge might encourage others to do so. We believe that it would be most appropriate to allow market forces to drive any such move. Given the difficulty that even the larger audit firms have experienced in engaging with listed company shareholders, we question whether there would be a large readership of Transparency Reports prepared by smaller audit firms.

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15	<i>Do you have any comments on the role of the FRC in this context [ie whom should own the Code]? (para 91)</i>	<p>We note that following the ministerial statements on 20 July on audit and audit regulation, the FRC is to take on the role of the single competent authority for audit regulation. It would therefore be logical for the FRC to “own” the Code in the future. We note, however, that with the additional powers assumed by the FRC should come additional accountability and oversight. In this context, we would expect the FRC to be accountable (perhaps to a Select Committee of Parliament) for the benefit and impact of changes made to the Code, and in particular the degree of prescription introduced.</p> <p>From a practical point of view, we would encourage the FRC to continue and increase its approach of collaborating closely with the profession in considering future changes to the Code.</p>
16	<i>Do you have any further comments on any of the issues raised in this report? (para 91)</i>	<p>We have no further comments.</p>