

FAO James Ferris

James – I wanted to share a few observations based on my interpretation of the FRC's proposed changes and its impact in the real world.

**Timing** – you propose introducing the standard for the audit of periods ending after 15 December 2019. This catches the majority of PIEs with a financial year end of 31 December 2019. With the guidance not yet finalised you are leaving a very short time period to introduce this. Our auditors have already planned their year end procedures. I would rather be running our business than working with auditors (& my international colleagues) to adapt their plans at short notice.

**Other reviews e.g., CMA** – Should other reviews require additional changes (potentially conflicting?) you risk asking us to do something for 2019 and then change once again for 2020. I suggest it would be better to align and consolidate changes across each of the reviews and implement them once. “Salami slicing” these changes will mean not just uncertainty amongst auditors but also amongst their clients who have to prepare the analyses for the auditors.

**White-list exclusions** – this excludes buy-side or sell-side due diligence work for all audit PIE's (which would include the private equity and investment banking operations of the main UK financial institutions). That reduces our choice in the market. It also encumbers the way we run sellside processes, often using our auditors to gather extra data to support a sale process without necessarily involving affected management at the early stages until we are certain of moving into a transaction.

**Anomaly re vendor due diligence** – VDD is a key part of M&A these days. We participate in many “auction processes” supported by a VDD report. The FRC's suggestion means if we now “win an auction” but KPMG (our auditors) had carried out the VDD, KPMG couldn't address the report to us. Likewise if I sell a business with a VDD I now have to consider whom they are audited by. Typically it is the bidder with the most industrial logic that wins out, not the one with an unconflicted auditor.

**Worldwide reach of the standard** – I believe the draft proposes that all services provided by the UK auditor and its network firms would be subject to the non-audit services restrictions. So, for instance, the US firm of a big 4 auditor couldn't perform due diligence services for a US parent of a UK PIE audited entity. I can't see how you'd expect a UK PIE to control decisions of its overseas parent.

**Private reporting accountant work** – in providing our management sign-offs on for instance working capital sufficiency, material adverse change or adequacy of extraction required when we issue equity or listed debt; or indeed should we ever do a UKLAClass 1 transaction then we gain comfort from our auditors review, their familiarity with the way we pull the numbers together and their “comfort letter” process. As do our Sponsors. We think our auditors are best placed to provide these services - often coterminous with issuing financial statements. If our auditors can't do this then there would be duplicate cost, inefficiency and complexity at a period when time pressure is already high. There is a natural “synergy” having auditors do this work that you would be denying us.

**Multiple auditors** – it's not uncommon to use more than one firm of auditors e.g., we may retain incumbent auditors after acquiring a business and have group auditors supplement the local processes for the first year. If the CMA's recommendation of having joint audits is ever enacted then the issue is exacerbated. In this case none of the Group's subsidiary auditors are able to provide prohibited services to its audit client's parent. This could lead to

us having very little choice - I like to choose my advisers based on quality & capability rather than availability.

So in summary, improving confidence in and the quality of an audit is a good thing but the exposure draft doesn't do that. Rushing its introduction risks major plcs such as ourselves trying to resolve "regulatory" problems rather than having our advisers add the value we pay them for.

**Chris Hunt**

Head of M&A