BAKER TILLY

First Floor, Quay 2
139 Fountainbridge
Edinburgh
Scotland, EH3 9QG
United Kingdom

T: +44 (0)131 659 8300
F: +44 (0)131 659 8301

www.bakertilly.co.uk

Our ref: TMM/AT
Your ref:

Keith Billing Esq
Financial Reporting Council
8th Floor
125 London Wall
London
EC2Y 5AS

20 March 2015

Dear Mr Billing

Consultation: Auditing and ethical Standards
Implementation of the EU Audit Directive and Audit Regulation

On behalf of the Group A firms and of the Association of Practising Accountants firms, we hereby submit this joint response to the above consultation paper.

The Group A firms are:

Baker Tilly
Smith & Williamson
Mazars
Moore Stephens
Saffery Champness
Haines Watts
Crowe Clark Whitehill
Kingston Smith,

and the Association of Practising Accountants firms are:-

Buzzacott LLP
Armstrong Watson
Reeves & Co. LLP
Price Bailey LLP
Blick Rothenberg LLP
Duncan & Toplis Limited
Mercer & Hole
James Cowper LLP
Shipleys LLP
Barber Harrison & Platt
Brebners
Dixon Wilson
Roffe Swayne.

The combined annual revenues of our firms are in excess of £1.1bn, and we have 1,411 partners and 11,216 staff, in over 230 offices spread throughout the UK.

We are pleased to offer our submission to this important debate and stand ready to deal with any questions you may have arising from our response.

Yours sincerely

T M McMorrow

T M McMorrow LLB LLM PhD
Director of Policy, Regulation and Ethics

Joint Group A and APA firms' response to the latest FRC consultation paper: *Auditing and ethical standards: Implementation of the EU Audit Directive and Audit Regulation.*

Executive Summary:

This response is joint between the Group A and the members of the Association of Practising Accountants (we have appended a list of all of the firms which have ascribed to the response), namely the medium sized firms that are active in the mid-tier market, including SMEs[1].

The Financial Reporting Council issued a high level consultation on 17 December 2014, setting out its preferences (in some instances offering a range of options), all predicated on the assumption that it will become the 'Single Competent Authority' under the new EU Regulation and Directive on audit reform. Whereas we have made a number of key points in relation to SCA operations in our parallel response to BIS' discussion paper issued on the same day, we respond below to the questions posited by the FRC and which, to one extent or another, read across to the other discussion paper. Both should be read together for that reason.

There are 27 questions in this consultation and the key areas they focus on, as identified by us, are whether:

- simplification could be applied in auditing and ethical standards for smaller company audits;
- the strictures and limitations in terms of professional and ethical standards that will apply to PIEs should be extended to other entities (for example, AIM);
- to go beyond the EU requirement of a prohibited black list of non-audit services (NAS) for PIE audits, and move to a 'white list' of permitted services for such audits;
- to extend such requirements outwith the UK;
- to extend the new 70% PIE NAS fee limits that apply to UK audit firms, to the whole audit network; and
- the audit firm should be responsible for ensuring firm rotation requirements are not breached.

Before turning our attention to the consultation questions themselves, we should like to make the following observations.

We note from the consultation paper (p5, para (xi)) and from what we have heard informally that the FRC intends to hold two further consultations on potential changes to the Ethical Standards for auditors in 2015. Given that the consultation paper is substantially about ethical issues, it would have been possible for the current paper to have given an indication of the likely nature of the changes considered necessary, or the policy-options favoured by the FRC: piecemeal or incremental regulation in a critical area should surely be avoided.

Our key observation, consistent with para 3.1 of the discussion paper[2], is that a true application of the principle of Proportionality would allow the FRC to take out a number of listed audit entities which do not present any level of systemic risk, allowing it to concentrate

[1] In total, we have annual revenues of £1.1bn+, with 12,600 partners and staff in 230+ offices around the United Kingdom..

[2] *"The definition of PIEs is therefore relevant to ensuring that the regulatory impact of the more stringent requirements of the Audit Regulation falls on all appropriate entities and is not higher than is necessary to preserve the public interest."*

on those that do. We therefore concur with BIS' view at para 3.6 of the consultation paper, that the EU definition of PIE should not be widened. Further, we do not accept the premise posited at para 3.7, that *"there are entities that do not automatically fall under the definition of PIEs…but are nonetheless of sufficient public interest to warrant applying to them some but not all of the more stringent requirements applicable to PIEs."*.

Given that UK regulation has no workable or well-understood definition of 'the public interest', we do not advocate the writing of regulations that give the appearance that it has[3]. We currently have no definition of public interest that is readily understood or applied and that this is an area that is creating significant debate in the UK profession and among other stakeholders, and we believe that there needs to be early debate on it: that definition will be seminal for many of the issues covered in the consultation.

Response to the List of Consultation Questions:

Question 1

Do you agree that the FRC should, subject to continuing to have the power do so after the Audit Directive and Regulation have been implemented, exercise the provisions in the Audit Directive and Audit Regulation to impose additional requirements in auditing standards adopted by the Commission (where necessary to address national law and, where agreed as appropriate by stakeholders, to add to the credibility and quality of financial statements)?

Yes, we agree that the FRC should be able to exercise the provisions in the Audit Directive and Audit Regulation to impose additional requirements in auditing standards adopted by the Commission *but only* in respect that it is necessary to do it to incorporate obligations into national law, not to 'super-comply' with/gold-plate those obligations. We accept that there may be instances where, it may make common sense among stakeholders, for the FRC to seek to impose additional requirements to add to the creditability and quality of financial statements but any additional requirements in this area should be kept to an absolute minimum: "gold plating" UK auditing standards is a very real danger, a consequence of which is to make UK auditors uncompetitive in the international market.

Rule-making of all kinds ought properly to be based on the principle consistent with other consultation processes conducted by the FRC, new obligations should be subject to impact assessment[4], the results of which ought to be made available to stakeholders ahead of formal consultation, consultation should be meaningful, and the FRC's responses to consultees' own responses thereafter made known and shown to be designed to achieve a clearly demonstrable and necessary solution to a clearly defined problem, at a proportionate cost: vague assertions that changes are designed to support or improve audit quality are insufficient.

We believe that the main strengths of the IAASB ISAs are that they are internationally consistent, and having been through a lengthy international public consultation process are accepted worldwide. Adding or deleting ISA requirements on a national basis only serves to distort the audit market and introduce arguably unnecessary differences, which combine to make it very hard to perform a consistent international group audit. Moreover, there can be problems around the effectiveness of communications between offices in countries, like the United States, that do not apply ISAs.

[3] The Appeal Tribunal in the case of *MG Rover Group* makes this point very clear in its Judgment.
[4] When new accounting standards are issued, they are accompanied by 'basis of conclusion' text.

We recommend that, if the FRC considers that auditing standards need to be augmented by additional requirements to add to the credibility and quality of financial statements, that those requirements are not implemented unilaterally by the FRC but that it should instead seek to lobby IAASB and the European Commission: this is an instance of the FRC needing to advocate change among international partners, not implement unilaterally. It should be mandatory for the FRC to exercise the power contained in Article 26(ii)(b) only in exceptional circumstances, on cause shown.

Question 2

Do you believe that the FRC's current audit and ethical standards can be applied in a manner that is proportionate to the scale and complexity of the activities of small undertakings? If not, please explain why and what action you believe the FRC could take to address this and your views as to the impact of such actions on the actuality and perception of audit quality.

We make a distinction between auditing standards and *ethical* ones. Whereas auditing standards do not present the same opportunities for simplification, the Ethical Standards for Auditors do.

This is recognised by the existing PASE provisions and we do not advocate any changes to those provisions[5]. The existing PASE provisions are sufficient to address 'small undertakings', using the definition of such under the Audit Directive, though the definition only covers *very* small undertakings. There is very little consistency in definitions between auditing standards and ethical ones, in particular how they apply to small entities.

We are talking, in this context, about measures being proportionate to the size of the entity that is being audited. There is a very important principle at play here and our opinion is that a sense of proportion should permeate the whole Regulation and Directive implementation exercise. in this context, we consider, with regard to ethical standards, that it would be helpful to consider whether they are currently being applied proportionately, insofar as certain publicly traded companies – e.g. those traded on AIM - that do not fall into the PIE definition are concerned: our view is that the FRC could quite properly introduce a deregulatory measure in the ESAs, by discontinuing the current distinction in definition between Listed and Non-Listed companies, and substituting one between 'PIE' and 'non-PIE'.[6]

To do so would be compatible with our belief that, as the articles concerned in Q2 (22b, 24a and 24b) relate to auditor independence, audit firms' internal organisation, and maintenance of records in relation to breaches/complaints, simplified requirements should not be made available: we *do*, however, support the proposition that allows the FRC to remove *current* gold-plating.

Question 3

When implementing the requirements of Articles 22b, 24a and 24b, should the FRC simplify them, where allowed, or should the same requirements apply to all audits and audit firms

[5] Even though few of our firms actually use them in ethical decision-making.

[6] It should be noted that to do so would also achieve greater consistency with the criteria that the AQR function of FRC currently uses itself anyway: it identifies what it terms a 'major audit' (by which it presumably means an entity in which there is significant public interest) by reference to whether that entity has a market cap of £100m or more. AQR therefore by definition accepts that there is little or no public interest in Listed companies below that market capitalisation. Enquiries made of AIM reveal that some 82% of the 1000+ entities registered on it are ‹£100m.

regardless of the size of the audited entity? If you believe the requirements in Articles 22b, 24a and 24b should be simplified, please explain what simplifications would be appropriate, including any that are currently addressed in the Ethical Standard 'Provisions Available for Small Entities', and your views as to the impact of such actions on the actuality and perception of audit quality.

Consistent with our response to Q2, there is an opportunity for the FRC to bring about significantly deregulatory measures, by taking AIM-listed (and similar such as ISDX) entities out of the most restrictive of ethical prohibitions. There is a sound public policy justification for such a measure as it would be entirely consistent with government Industrial Strategy and the Growth imperative, giving companies with the most need yet the greatest potential the opportunity of accessing professional advice in respects they currently cannot. This recommendation does not impinge on the actuality or perception of audit quality because it fully reflects the legal requirements in the UK, and the monitoring of the audits of those companies will remain in place.

Articles 22b, 24a and 24b set out aspects in which Member States are entitled to simplify the audit of 'small undertakings'. We believe the requirements of Articles 22b, 24a and 24b should be applied to all audits and audit firms except the requirements under Article 24a in respect of remuneration policies and performance policies.

Question 4

With respect to the more stringent requirements currently in the FRC's audit and ethical standards (those that are currently applied to 'Listed entities' as defined by the FRC) that go beyond the Audit Directive and Regulation:

(a) should they apply to PIEs as defined in the Audit Directive?

(b) should they continue to apply to some or all other Listed entities as currently defined by the FRC? If so, which of those requirements should apply to which types of other Listed entities?

No, we do not recommend that the FRC imposes additional requirements on PIEs beyond those set out in the EU Audit Directive and Audit Regulation. We believe that the current Ethical Standards are trapping a wider population of entities than is either necessary or desirable. We do not believe that the FRC should be "gold plating" auditing and ethical standards except where this is required by national law or, in very exceptional circumstances, is considered necessary to add to the credibility and quality of financial statements. Nor do we believe that the provisions of the Ethical Standards for Auditors' provisions as they relate to <u>all</u> Listed companies should continue: AIM-listed (and similar, e.g. ISDX) companies, as we made clear above, should not be subject to the prohibitions attaching to Listed entities - in our opinion the FRC needs to consult and agree upon a definition of a PIE that is appropriate to the UK market and we recommend that the FRC follows the approach adopted in the EU and exclude AIM-listed, and similar, entities from the definition of a PIE in the UK. There are, as we pointed out above, sound public policy reasons underpinning our recommendation, and specific comment is included in our further responses below.

Moreover, we point up an inconsistency in the way that the FRC, on the one hand, approaches auditing standards and ethical standards so far as the definition of PIE/major audits is concerned, and, on the other hand, with the audits that it identifies as having 'public interest' characteristics when it comes to monitoring: AIM-listed companies are not within the scope of the enhanced audit reporting regime but are brought into the scope of the Ethical Standards for Auditors.

Para 3.2 of the consultation paper says that "[*t]he definition of PIEs is therefore relevant to ensuring that the regulatory impact of the more stringent requirements of the Audit Regulation falls on all appropriate entities and is not higher than is necessary to serve the public interest.*". In para 3.7, the FRC says it agrees with the BIS proposal not to widen the EU definition of PIEs for implementation purposes, but then goes on to propose doing exactly that for entities of "*sufficient public interest*", applying to them "*some but not all of the more stringent requirements applicable to PIEs.*". Using the public interest as a yardstick for applying and disapplying requirements will lead only to an inconsistency of approach. We believe that the inconsistency we are describing comes from the misalignment between entity-definitions and audit monitoring ones.

Departure from the requirements of the Regulation would also create another dimension of inconsistency - in how the rules are applied among Member States: companies may be incorporated in one country but have securities listed in another, for example.

Inconsistency breeds complexity and unevenness of application of standards. It is on avoiding regulatory unevenness that our submissions are based: we are seeking to capitalise on the work that the FRC has done in the auditing and ethical standards space, remove domestic and international inconsistencies, and support the interests of investors and other stakeholders.

BIS' conclusion (as cited above) is correct and represents the best option going forward; the FRC may depart from it only on the most persuasive of evidence.

Question 5

Should some or all of the more stringent new requirements to be introduced to reflect the provisions of the Audit Regulation apply to some or all other Listed entities as currently defined by the FRC? If so, which of those requirements should apply to which types of other Listed entities?

No, we believe that the FRC should agree first on a UK definition of a PIE which is consistent with the extent of legal obligation, avoiding the extension of current restrictions that obtains presently (and picking up the observation we made above, that AIM and ISDX-listed entities should be scoped out of the definition). Then if there any more stringent requirements to be introduced to reflect the provisions of the EU Audit Regulation, these should be applicable to UK PIEs on a consistent basis.

Question 6

Should some or all of the more stringent requirements in the FRC's audit and ethical standards and/or the Audit Regulation apply to other types of entity i.e. other than Listed entities as defined by the FRC, credit institutions and insurance undertakings)? If yes, which requirements should apply to which other types of entity?

No, as stated above, we do not recommend that the FRC imposes more stringent requirements on UK PIEs beyond those set out in the EU Audit Directive and Audit Regulation.

Question 7

What approaches do you believe would best reduce perceptions of threats to the auditor's independence arising from the provision of non-audit services to a PIE (or other entity that may be deemed of sufficient public interest)? Do you have views on the effectiveness of (a) a 'black list' of prohibited non-audit services with other services allowed subject to evaluation of threats and safeguards by the auditor and/or audit committee, and (b) a 'white list' of allowed services with all others prohibited?

Proportionality, as paragraph (viii) of the Introduction to the consultation paper makes clear, is the guiding principle for any changes the FRC seeks to introduce. It would have been helpful if we could have been apprised of the likely direction of travel for the two further consultations on ethics expected this year, as it is always better to avoid an incremental approach to standard-setting, especially when it is clear from para 4.10 that, *"The FRC is considering whether it is necessary or appropriate to exercise the Member State option to prohibit additional non-audit services to address concerns about…threats to auditor independence."*.

The IESBA Code, with which the ESAs are fully consistent, and the threats and safeguards approach it advocates, is still contemporarily relevant and needs no elaboration, save to address any ambiguities): the checks and balances embodied in the ESAs protect the public interest and are designed to be applied in a principles-based way, avoiding prescription. We believe that, provided it is based primarily on the prohibitions currently contained in the ESAs, together with any purposive further prohibitions contained in the Regulation, the establishment of a "black list" of prohibited non-audit services will best reduce perceptions of a threat to auditor independence. It seems to us that the black list arguments set out at paras 4.16 to 4.22 are highly persuasive and representative of sound government and Competition & Markets Authority aims and beliefs. On the other hand, we believe that a "white list" approach needs very much to be avoided as it introduces an unacceptable degree of subjectivity as to where the margins of acceptability lie.

The advantage of a "black list" is that it will establish clearly which non-audit services are prohibited but will also mean that audit committees maintain some involvement and discretion in determining whether it is appropriate for the statutory auditor to carry out non-audit services which are not included on the black list. We believe that the "black list" approach is consistent with the current UK system of threats and safeguards which has worked well for many years and allows judgement to be applied when deciding whether non-audit services can be provided, allowing for safeguards to be adopted to protect independence.

Although we see the possibility that a white list might also be so drafted as to express the corollary of the black list, there may be a large grey area between the content of each, where adopting the UK system of threats and safeguards would have produced a more sensible outcome. The creation of a white list also runs the risk that non-audit services will be undertaken by the statutory auditor where, in the specific circumstances concerned, it is not appropriate to do so.

We make the further point that there should be explicit acceptance on the part of the FRC that the black list applies only to PIEs and gives an undertaking that it will not be extended further.

Question 8

If a 'white list' approach is deemed appropriate to consider further:

(a) do you believe that the illustrative list of allowed services set out in paragraph 4.13 would be appropriate or are there services in that list that should be excluded, or other services that should be added?

(b) how might the risk that the auditor is inappropriately prevented from providing a service that is not on the white list be mitigated?

Please see our response to Question 7 above – we consider that the establishment of a black list rather than a white list is more appropriate.

Question 9

Are there non-audit services in addition to those prohibited by the Audit Regulation that you believe should be specifically prohibited (whether or not a 'white list' approach is adopted)? If so, which additional services should be prohibited?

There are no further non-audit services which we consider should be prohibited by the Audit Regulation, and nor do we advocate the introduction of any additional degree of restriction within current prohibitions.

Question 10

Should the derogations that Member States may adopt under the Audit Regulation – to allow the provision of certain prohibited non-audit services if they have no direct or have immaterial effect on the audited financial statements, either separately or in the aggregate - be taken up?

We agree in principle that where a non-audit service has no direct impact or brings about merely an immaterial effect on the financial statements, it could be carried out subject to the other relevant considerations concerning independence. However, we believe that applying this principle in practice will be difficult. For example, in the case of valuation work, the valuation will, in all likelihood, have to be completed before an assessment of materiality can be made.

Question 11

If the derogations are taken up, is the condition that, where there is an effect on the financial statements, it must be 'immaterial' sufficient? If not, is there another condition that would be appropriate?

No, in addition to the requirement for the impact on the financial statements to be immaterial, we consider that the nature of the work to be performed and the extent of subjectivity that it involves should be considered. For example, where payroll services are to be provided (which we note are not on the list of prohibited services which may be allowed by derogation), there is minimal, if any, judgement exercised whilst valuation work which (often, though not always) does entail a significant level of subjectivity and judgement is on the list of prohibited services which may be allowed by derogation. The obvious inconsistency is brought about because payroll services fall within the definition of 'accounting services', itself a prohibition where Listed companies are concerned. The provision of payroll is largely a mechanical exercise and as such avoids the self-review threat. Provision of payroll ought to permitted under the ESAs even as currently drawn. Material (not, please note, immaterial) valuations may present such a compromise.

Question 12

For an auditor to provide non-audit services that are not prohibited, is it sufficient to require the audit committee to approve such non-audit services, after it has properly assessed threats to independence and the safeguards applied, or should other conditions be established? Would your answer be different depending on whether or not a white list approach was adopted?

Yes, we believe that the audit committee's consideration of whether or not non-audit services should be provided by the statutory auditor, alongside the existence of a black list is sufficient.

Question 13

When implementing the provisions of the Audit Regulation in the Ethical Standards, should the FRC require the group auditors of PIEs to ensure the principles of independence set out in the FRC's standards (including the provisions relating to the provision of non-audit services) are complied with by all members of the network whose work they decide to use in performing the audit of the group, with respect to all components of the group based wherever based? If not, what other standards should apply in which other circumstances?

Provided that we are dealing with audit firms in the same network (it is not necessary if the auditor of the subsidiary is not in the same network as the group auditor), yes, in order to maintain public confidence in the auditing profession, we believe that the group auditor should ensure that the principles of independence set out by the FRC are complied with by all group auditors regardless of where they are based or whether they are part of the same network. Where other group auditors are based in the EU, compliance will be easier to establish than when they are based outside the EU but this does not mean that the principles of independence should not be complied with across the board. It ought to be borne in mind, however, that the ideal we have just expressed can be difficult to achieve in practice and that absolute responsibility on the part of the group auditor may bring about unfairness for minor or immaterial breaches of ethical standard. We therefore believe that the FRC ought, in the two further consultations on the ESAs to take place this year, to consult on the practicalities of the general proposition.

Question 14

When implementing the provisions of the Audit Regulation in the Ethical Standards, should the FRC require the group auditors of PIEs to ensure the principles of independence set out in the FRC's standards (including the provisions relating to the provision of non-audit services) are complied with by all other auditors whose work they decide to use in performing the audit of the group? If not, what other standards should apply in those circumstances?

Yes. Please see our response to Question 13, and the proviso where the auditor of the subsidiary is not in the same network as the group auditor. In the case of *non*-network subsidiary auditors, we are unpersuaded that it is appropriate to lay on the shoulders of the group auditor an obligation effectively to certify the subsidiary auditor's independence. Apart from the question of onus, to so do would necessarily mean subordinating the ethical judgment of the subsidiary's auditor to that of the group auditor. That, we respectfully argue, is a recipe for professional dispute and impugns the subsidiary auditor's professionalism. Obliging the group auditor to be satisfied about the subsidiary auditor's independence is the middle-way we would recommend.

Question 15

Is the 70% cap on fees for non-audit services required by the Audit Regulation sufficient, or should a lower cap be implemented for some or all types of permitted non-audit service, including the illustrative 'white list' services set out in Section 4?

Yes, we believe that the 70% cap on fees for non-audit services required by the Audit Regulation is sufficient. We regard such a cap on fees and the *nature* of the non-audit services provided to be two separate issues. For example, if, under local legislation, a non-audit service is required to be carried out by the statutory auditor, we consider that it should still be included in the overall calculation of audit fees versus non-audit fees.

We believe too that the FRC ought to conduct research on how competition principles might be advanced, by causing firms other than the largest to be invited to tender for provision of those non-audit services that audit firms might have to decline by operation of the cap.

Question 16

If the FRC is made the relevant competent authority, should it grant exemptions from the cap, on an exceptional basis, for a period not exceeding two years? If yes, what criteria should apply for an exemption to be granted?

Yes, we consider that the FRC should be able to grant exemptions on an exceptional basis for a period not exceeding two years as set out in Article 4 of the Audit Regulation. Care would have to be taken that an 'exceptional circumstances' derogation did not become the default position, however. It follows that it may be instructive for the FRC to consult on the sorts of circumstance that would be acceptable under the derogation, codifying wording in the revised ESAs.

Question 17

Is it appropriate that the cap should apply only to non-audit services provided by the auditor of the audited PIE as required by the Audit Regulation or should a modified cap be calculated, that also applies to non-audit services provided by network firms?

As set out in our response to Question 13, the group auditor should establish whether all other group auditors (provided they are in the same network, not if otherwise) have complied with the FRC's principles of independence which includes considering the level of audit versus non-audit fees, but we are not unanimous in this view; some of our firms believe that obligations in relation to the cap should apply only to PIE auditors rather than the whole network (as a means of avoiding unnecessary gold-plating). In the light of this we do not believe that further consideration of audit versus non audit fees is required at network level, given the nature of the remuneration structures generally seen in networks.

Question 18

If your answer to question 17 is yes, for a group audit where the parent company is a PIE, should the audit and non-audit fees for the group as a whole be taken into consideration in calculating a modified alternative cap? If so, should there be an exception for any non-audit services, including the illustrative 'white list' services set out in Section 4, be excluded when calculating the modified cap?

Please see our response to Question 17 above.

Question 19

Is the basis of calculating the cap by reference to three or more preceding consecutive years when audit and non-audit services have been provided by the auditor appropriate, given that it would not apply in certain circumstances (see paragraphs 5.3 and 5.15)?

Yes, we believe that the calculation of the cap by reference to three or more preceding consecutive years when audit and non-audit services have been provided by the auditor appropriate.

Question 20
Do you believe that the requirements in ES 4 should be maintained?

No, we consider that the fee limits set out in Paragraph 3 of Article 4 of the Audit Regulation are appropriate and therefore that the more stringent requirements of ES 4 should not be maintained. We do not believe that the requirements applicable in the UK should be more stringent than those applicable in other Member States in order that the UK does not become uncompetitive. We therefore fundamentally disagree with the FRC's assertion in para 5.21 that, *"…it is appropriate to maintain the long standing more restrictive requirements in ES4"*, and in the event that the FRC wishes to maintain the requirements, then they should be disapplied to AIM,etc –listed entities.

Question 21
When the standards are revised to implement the Audit Directive and Regulation, do you believe that these more restrictive requirements in ES 4 should apply with respect to all PIEs and should they apply to some or all other entities that may be deemed to be of sufficient public interest as discussed in Section 3? If yes, to which other entities should they apply?

No, please see our response to Question 20 above.

Question 22
Do you believe that an expectation that fees will exceed the specified percentages for at least three consecutive years should be considered to constitute an expectation of "regularly" exceeding those limits? If not, please explain what you think would constitute "regular".

We do not consider that the more onerous provisions of ES 4 are appropriate. However, in the event of removing any forward looking review of audit vs non audit fees, our concern is whether there is scope for potentially significant future non-audit fees which are close to being secured being ignored.

Question 23
Should the FRC stipulate a minimum retention period for audit documentation, including that specified by the Audit Regulation, by auditors (e.g. by introducing it in ISQC (UK and Ireland) 1)? If yes, what should that period be?

Yes, we believe that the UK should be bound by the same requirements in this area as other Member States and consider that a 5 year retention requirement, as set out in Article 15 of the Audit Regulation, is appropriate. The RSBs have recommendatory time-periods which correspond with the short, negative prescription limits in law, and the FRC may be minded to maintain the obligations in this respect in line with RSB requirements, which would have the benefit of amendment-flexibility.

Question 24

Do you believe that the FRC's audit and/or ethical standards should establish a clear responsibility for auditors to ensure that they do not act as auditor when they are effectively time barred by law from doing so under the statutory requirements imposed on audited PIEs for rotation of audit firms?

Yes, in order to maintain public confidence in the auditing profession, the FRC's audit and/or ethical standards should establish a clear responsibility for auditors to ensure that they do not act as auditor when they are time barred from doing so.

Question 25
Do you believe that the requirements in ES 3 should be maintained?

No, we believe that the requirements of Article 17 of the Audit Regulation in relation to rotation of audit principals should be applied rather than those set out in ES 3. This is not only to ensure consistency with other Member States but also because rotation after 7 years followed by at least 3 years of not being involved with the client is more likely to result in true rotation of audit principals than the current regime in the UK which allows a cyclical '5 years on, 5 years off'.

The number of years before rotation is actually quite arbitrary, and what *really* matters is the need for auditors to avoid 'capture'/too close an alignment with management. Our suggestion that the period ought to be 7+3 is not regressive in this respect; it more appropriately tempers the objectivity/'capture' equation and will contribute, we believe, beneficial results from an Audit Quality perspective.

The FRC should not be gold-plating in this area, especially in the absence of any evidence that UK auditors are any less independent and require stricter rules.

Question 26
When the standards are revised to implement the Audit Directive and Regulation, do you believe that these more restrictive requirements in ES 3 should apply with respect to all PIEs and should they apply to other entities that may be deemed to be of sufficient public interest as discussed in Section 3? If yes, to which other entities should they apply?

No, please see our response to Question 25 above.

Question 27
Are there any other possible significant impacts that the FRC should take into consideration?

During the course of our review of the FRC Consultation we have not noted any further possible significant impacts that the FRC should take into consideration. The implementation process presents an opportunity, which we urge the FRC to take, to establish itself as a regulator recognised for its adherence to 'regulatory best practice' principles and exhibiting constant regard for the principle of proportionality.

The Group A and Association of Practising Accountants firms