



Grant Thornton

An instinct for growth™

Financial Reporting Council
8th Floor
London Wall
LONDON
EC2Y 5AS

Grant Thornton UK LLP
Grant Thornton House
Melton Street
London NW1 2EP.
T +44 (0)20 7383 5100
F +44 (0)20 7383 4715
DX 2100 EUSTON
www.grant-thornton.co.uk

12th February 2016

Dear Sirs

Draft Plan & Budget and Levy Proposals 2016/17

Grant Thornton UK LLP (Grant Thornton) welcomes the opportunity to comment on the Financial Reporting Council's (FRC) Draft Plan & Budget and Levy Proposals 2016/17 published in December 2015.

We support the FRC's mission to promote high quality corporate governance and reporting to foster investment. In our view the outcome of a good regulator is a clear and transparent framework to provide market confidence in auditing, corporate governance and reporting and our comments are made with this in mind.

In summary our key messages are:

- We strongly believe the right way for the FRC to achieve its mission is by adopting a principles-based approach to regulation. The badge of "public interest" should not be seen to conflict with a regulatory approach that is fair, proportionate and evidence-based.
- We are concerned that there a number of statements in the proposals that, prima facie, are consistent with increasing, not reducing, regulatory intervention and we question whether the FRC's own evidence supports the need for a "step change" in audit quality.
- The overlay by FRC of additional requirements on top of EU and international frameworks can become unwieldy, cumbersome and costly for businesses, audit firms and investors alike and can cause confusion in the global market.
- The need for a balanced approach to change is very much brought into focus by the forthcoming implementation of the EU Regulation and Directive on Audit Regulation and the need attract and retain talented people.
- We very much favour speedier resolution of disciplinary matters which can at the moment drag on for many years, consuming much time and resource and prolonging the stress for the individuals involved.
- We expect the FRC to approach its management of costs as do the businesses and audit firms it regulates.
- We question whether it is it appropriate for the profession to fund the whole of the audit standard-setting and regulatory costs.

We set out below our comments in more detail.

General comments on regulatory approach

In fulfilling its mission we strongly believe the right way for the FRC to achieve this is by adopting a principles-based approach to regulation. In this respect, we very much welcome some of the over-arching comments in the proposals concerning the FRC's "support for an effective and proportionate regulatory framework" and the adoption of an approach that is "in line with the Government's initiative to reduce regulatory burdens on business".

However, we are concerned that there a number of other statements in the proposals that, prima facie, are consistent with increasing, not reducing, regulatory intervention, which arguably is not necessary and may prove to be dis-proportionate. For example, the FRC expresses its goal to ensure that reporting and audit in the UK are "world-leading" and that it will concentrate on promoting a "step change in audit quality". The first of these statements might imply a continuation of "gold-plating" of EU and international standards. There is an implication here that the UK will always "front run" the international debate but at some point we would expect the FRC to recognise that, if there has been sufficient debate internationally, then there should be alignment. The continuation of different regulatory regimes and the overlay of additional requirements on top of EU and international frameworks can become unwieldy, cumbersome and costly for businesses, audit firms and investors alike and can create confusion in a global market.

The second of these statements regarding a step change in audit quality also implies that this is needed to bring the audit quality in the UK up to an acceptable standard. This seems to be inconsistent with the findings of the FRC 's recent survey of Audit Committee Chairs (ACCs) which notes that feedback from ACCs on audit quality was "overwhelmingly positive", and that ACCs scored their auditors highly across all questions. Furthermore, the FRC noted in its 2013/14 annual report that the quality of auditing in the UK is "generally good, most notably in relation to the very largest listed companies" and in its subsequent 2014/15 report that the "quality of individual audits continued to show an improvement". We recognise that as an audit firm we must continually strive for improvement, which is in line with the FRC's comment in its own effectiveness review calling for a regulatory stance that "promotes continuous improvements in standards of reporting and auditing". However, this does not imply "step change" is necessary, especially when seen in the context of the FRC's stated objective that "it will not seek to change the codes and standards.... for at least the remainder of the 2016/19 period, and longer, if possible".

The need for a balanced approach to any changes is further brought into focus by the forthcoming implementation of the EU Regulation and Directive on Audit Regulation which will be introduced into the UK in 2016. The introduction of the new regulatory framework, and in particular the revisions to the ethical standards, will bring about significant change for auditors and the companies they audit. Whilst most changes proposed are inevitable, as they as required by legislation, some of the practical and transitional implications remain uncertain. When implementing these new arrangements in the UK, we urge the FRC to do so in a way that is consistent with an effective and proportionate regulatory framework.

Also in this context we believe that the FRC shares a responsibility to ensure the auditing profession is one which can attract and retain talented people. This important factor very much reinforces the need for a balanced approach to the implementation of further change, so as to avoid any potential longer term negative impact on the quality of people joining and wanting to stay in the profession. The standards of a regulatory and professional framework should be such that quality people aspire to be a part of it, rather than being put off by it.

The FRC makes it clear in its proposals that, in carrying out its mission, it needs to act "in the public interest". We agree with this and fully acknowledge our own public interest responsibility. Indeed at Grant Thornton the recognition of this wider responsibility is specifically incorporated in the terms of reference of our Partnership Oversight Board, the body responsible for standards of corporate governance within the firm. However, we think it is important that the badge of "public interest" should not be seen to conflict with an

approach that is fair, proportionate and evidence-based. To promote best practice, as is its stated aim, we need a regulator that adopts an inquiring, learning and evolving approach, rather than an adversarial one, and promotes transparency and collaboration.

Other comments

Corporate reporting

We support the FRC's intention to focus on helping smaller listed and AIM companies with the quality of reporting and look forward to seeing more detailed proposals in this regard. As auditors we have a role to play in improving the quality of reporting but ultimately the auditor's key point of leverage is of a compliance nature to ensure that financial statements meet the true and fair threshold. To achieve real progress in this area requires preparers of financial statements to be convinced of investors' interest. With this in mind, the FRC's recent report on "Improving the Quality of Reporting by Smaller Listed and AIM companies", which emphasised the high level of investor interest in the quality of annual reports, was very helpful. This message needs continual re-enforcement. In this respect, we support the FRC's planned initiative to implement a new strategic stakeholder communications programme and enhance the degree of investor involvement in its work.

The planned move to name in advance a small proportion of reports and audits the FRC intends to review is potentially a welcome innovation in the interests of transparent regulation. However, as this is quite a significant change from the existing regime we very much support its introduction by way of a pilot so as to identify any potentially unintended consequences and constraints before any full implementation.

Audit

The FRC notes that, in directing its quality review activities in line with the new regulatory framework, it will focus "more strongly on identifying and promoting good practice" and "supporting innovation by the profession". We very much support such an approach and look forward to seeing developments in this area. In this connection we suggest the AQRT reviews its approach to achieve this goal, as historically its work and the resulting reports have focussed on matters where it considers the quality of the work undertaken is below the standard expected.

Disciplinary regime

We note that the FRC will strive to take enforcement action in "a timely and cost-effective way" and that it aims to complete investigations of accountants and actuaries after no more than two years on average. We very much favour speedier resolution of such matters which can at the moment drag on for many years, consuming much time and resource and prolonging the stress for the individuals involved. We therefore welcome the aim to shorten the period of investigation. We take it that the objective of completing investigations within an average of two years is intended to start with the referral of the conduct by the Conduct committee to Executive Counsel for investigation under Paragraph 7(4) of the Accountancy Scheme and end with either settlement under paragraph 8 of the Accountancy Scheme, or the findings of the tribunal. We raise this point because the FRC refers to the starting point as the passing of the "formal complaint" to Executive Counsel and our understanding is that a formal complaint is delivered to a the member *following* investigation by Executive Counsel.

Cost and Budgetary matters

Generally on costs we would expect the FRC to approach its work as do the businesses and audit firms it regulates: to use a risk based approach, making good use of technology, with a rigorous focus on efficiency in the way it carries out its projects and fulfils its responsibilities.

It is not immediately clear to us what is meant by “our work in audit” (page 23) and therefore why it is “inappropriate” for corporate and other funding groups to contribute. If this work covers, for example, the setting of auditing standards and related international activities, given that high quality audits (based on high quality standards) are of benefit beyond the profession, we question whether it is appropriate for the profession to pick up the whole of the related cost?

In this context we note that Article 21 of the EU Regulation on audit reform states that “The funding of [competent authorities] shall be secure and free from undue influence by statutory auditors and audit firms”. If the competent authority is funded entirely or substantially by the those entities that it regulates, then there could be a risk to the public perception of the independence of the regulator and some stakeholders may view the funding mechanism as a disincentive to appropriate regulatory action. The solution to this problem lies in broadening the body of market participants that contribute to the FRC’s funding. In so doing we believe that more market participants will engage with the FRC around its work programme, its communication, and its output. Broader engagement would better inform and focus the work of the FRC, and promote greater use by stakeholders of its output.

From the tables on pages 21 and 23 it would appear that the audit professional bodies pay the entire cost of the Accountancy Disciplinary Cases (budgeted at £5m for 2016/17). However, the total contribution by the actuarial profession only appears to cover half of the costs of actuarial cases. We question the logic of this apparent discrepancy.

In terms of areas for potential cost or efficiency savings, we question whether the FRC needs to respond independently to IASB discussion documents, rather than contributing to the debate through feeding into EFRAG responses, and only responding separately if there is strong disagreement with the EFRAG response. We appreciate that FRC might not want to go down this route if other European standard-setters continue to submit individual responses but it could consider taking some initiative in that direction by only submitting separate comments on areas where it feels most strongly and disagrees with EFRAG.

Contact details

If you have any questions regarding this response, please contact me or Andrew Vials (t: 020 7728 3199; E: Andrew.Vials@uk.gt.com).

Yours faithfully



Sue Almond
Head of Assurance
For Grant Thornton UK LLP

T (0)207 728 2201
E sue.almond@uk.gt.com