



Grant Thornton

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Dear Ms Horton

Enhancing Confidence in Audit The Financial Reporting Council's Audit Enforcement Procedure

Grant Thornton UK LLP ("Grant Thornton") welcomes the opportunity to comment on the Financial Reporting Council's ("FRC") consultation on the new Audit Enforcement Procedure ("the Procedure").

General comment

We acknowledge that the new Procedure is being introduced as a result of EU legislation on which the FRC is obliged to act. We also support the need for an appropriately strong system of enforcement and sanction so that the market can have confidence in audit. However, as we note below, there are elements of the new Procedure which could potentially lead to a much greater number of investigations and disciplinary actions. We would be concerned if this were to be the case, and observe that a move in this direction could have a long term detrimental effect on the ability of the profession to attract and retain talented people. Accordingly, as a general comment, we urge the FRC to bear this in mind when implementing the Procedure and to do so in a balanced and proportionate way, avoiding unnecessarily intrusive regulation.

Threshold for investigation

We note that the Procedure is intended to set out the mechanism for investigating breaches of a "Relevant Requirement." Although the final form of the Statutory Auditors and Third Country Auditors Regulations 2016 ("SATCAR 2016") has yet to be published, we understand that the Relevant Requirements will, at least in part, focus on breaches of the provisions of the Auditing Standards. This seems to be a very low threshold if applied to compliance with each and every provision of an auditing standard, rather than on the overall quality of an audit. It could potentially increase significantly the number of investigations if applied literally. We acknowledge that there is scope for dealing with a case through "constructive engagement" at the case examiner stage. However, paragraph 12 of Appendix B suggests that this will be "suitable where there has been a minor technical breach of the Relevant Requirements." This appears to be a very low threshold indeed and we would be concerned if it became the working assumption that such breaches were always worthy of wider investigation. Indeed, we question whether breaches of this nature are worthy of examination in the first place and we certainly would urge the FRC to avoid using the constructive engagement process as means of prosecuting minor technical breaches that are not symptomatic of a wider, more serious issue.

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This point is especially important in light of the AQR process, which is likely to uncover breaches of Relevant Requirements that the FRC could then consider under the Procedure. In this respect, it would be helpful if there was clarification on the interaction between the AQR process and the Procedure.

Threshold for enforcement action

Under the Procedure, the Conduct Committee will, when deciding whether a matter should be investigated, consider whether there is "a good reason" to do so. We believe that, similarly, the FRC should bring enforcement action against a statutory auditor only if there is a good reason to do so. Insignificant or unimportant breaches of Relevant Requirements should not be subject to disciplinary action under the Procedure without good reason. Given the importance of this criterion, we believe that the requirement for a good reason should be stated in the new rules.

Relationship between the new Procedure and the Accountancy Scheme etc.

The future relationship between the Procedure and the existing Accountancy Scheme is currently not clear. In particular

One of the principles underlying the design of the new Procedure is that there be a single, streamlined procedure to deal with the full range of audit enforcement. In these circumstances, we think that it would also be helpful if the FRC were to clarify whether and how the Accountancy Scheme will continue to operate at the time that it publishes the new Procedure.

We think that the FRC should confirm whether it will in future apply the Accountancy Scheme to public interest cases other than statutory audit work, or whether it will be discontinued.

We note that in many non PIE cases the FRC will delegate regulatory responsibility to the professional bodies. We assume that the professional bodies will deal with such matters within their existing disciplinary frameworks. However, it would be helpful if the interactions between the FRC and the professional bodies could be clarified, including the criteria that the FRC will apply when deciding whether to consider statutory audits of non PIEs under the Procedure rather than refer them to the relevant professional body.

Different frameworks for statutory auditors and members in business

At present, in appropriate cases, the FRC considers the conduct of both statutory auditors and members in business under the Accountancy Scheme. In appropriate cases, the FRC has under the Accountancy Scheme made findings of misconduct against both statutory auditors and members in business arising from the same circumstances.

It appears that under the Procedure, however, the FRC will hold statutory auditors to much stricter standards, such that any breach of a Relevant Requirement may lead to disciplinary action. Even if the FRC continues to run the Accountancy Scheme, the test that it provides for disciplinary action against members in business will be the higher threshold of misconduct. It seems inevitable that, in cases of comparable culpability between them, the FRC might in future take disciplinary action against the statutory auditor but not necessarily the members in business. This does not seem fair and could lead to inconsistent outcomes. It will also inevitably suggest to members in business that the standards to which they are held are lower than those applicable to the statutory auditors. There seems to be little rationale in this distinction and we suggest that the FRC explores whether there should be a parallel, rather than a different, scheme for members in business arising from the same set of circumstances.

Publicity for individuals

We consider that the Procedure should clarify the circumstances in which the FRC will announce publicly that individual members are under investigation. Such investigations can have a negative effect on a member's professional career, irrespective of the subsequent outcome of the case, and can also be immensely stressful for the individual concerned, especially where the investigation extends over a long period. Although we acknowledge that the name of the relevant individual can often be found elsewhere in the public domain, the profile of an announcement by the FRC is much higher.

While we recognise that there are cases where the engagement partner's conduct will be deserving of sanction, we think that it would be preferable if, under the Procedure, only the firm were to be placed under investigation in the first instance in order that the role of the engagement partner can be properly considered so that, taking into account all factors including the impact on the individual referred to above, an informed decision can be taken as to whether it would be appropriate for the individual also to be placed under investigation and a public announcement to that effect made.

Eligibility to sit on the Case Management Committee, etc.

We note that members who have current or recent experience of performing statutory audits are ineligible to sit on the Case Management Committee, the Tribunal and the Appeal Tribunal. We believe that many such persons are especially well qualified to determine whether there has been a breach of Relevant Requirements. In dealing with this issue, the EU Regulation refers to "members of the governing body, or responsible for the decision making, of [those] authorities." Accordingly we think that the FRC should consider whether this restriction necessarily applies to all elements of the Procedure, in particular at the Tribunal stage.

Requiring documents from third parties

We note that the FRC will now have statutory power to obtain documents from third parties. We consider this a positive development but are concerned that in practice it could prove very onerous for those receiving such a notice, particularly, for example, office holders of insolvent companies who generally hold many such appointments. We have had experience in the past, when public bodies have, without any suggestion of wrongdoing on our part, required this firm to perform disclosure exercises on which we have spent thousands of hours. The costs and dislocation to individuals and businesses of such requests should not be overlooked and we therefore urge the FRC to use this power sparingly and in a way that it not unduly onerous.

Time-limits

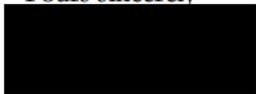
We ask that consideration be given to the inclusion of time limits, which could be extended in appropriate cases, by which the FRC will begin and conclude its investigations. There have been cases in the past under the Accountancy Scheme of long delays in the investigatory process.

As to the time limits in the Procedure for respondents to take various steps, we ask that the Executive Counsel be given the power to extend them in more complex cases, when more time may be needed.

Contacts

If you have any questions on our response, or wish us to amplify our comments, in the first instance, please do contact me or Andrew Vials (tel: 020 7728 3199, email: andrew.vials@uk.gt.com).

Yours sincerely



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