Via Email

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Dear Mr. Grewe:

Consultation Document: Monitoring the Work of Third Country Auditors

Grant Thornton International Ltd (Grant Thornton) welcomes the opportunity to comment on the above-referenced consultation document. This consultation by the Professional Oversight Board (POB) is directly relevant to our network of firms in over 100 countries, as we currently have three member firms registered with the POB, which includes one equivalent auditor (Australia) and two Article 45 auditors (Kuwait and Zimbabwe).

As regulators around the world are becoming more active in auditor oversight, many of them are also regulating foreign audit firms. In addition to the 27 EU Member States, we are now aware that the following countries impose (or are in the process of imposing) some sort of oversight or registration requirement on foreign auditors: Canada, Japan, Malaysia, New Zealand, South Africa and the United States. These requirements impose significant costs on regulators, audit firms and companies, and often result in duplicative oversight on audit firms. Perhaps more importantly, overlapping oversight can often put audit firms in an untenable position when the laws of different countries conflict and compel opposing actions.

To be clear, we firmly support independent oversight of audit firms, and believe that it contributes to both audit quality and also the public's and investors' confidence in the audit process. We believe, however, that the best way to realize the benefits from independent oversight – while minimizing unnecessary costs to regulators, audit firms and participants in the audit process – is for regulators to cooperate with one another to the maximum extent possible.

This cooperation should involve working together on registration and inspections conducted by home country oversight bodies. This cooperation and reliance would not only reduce costs to regulators, audit firms and companies, but would also enable regulators to:

- utilize the monitoring and enforcement efforts of the home country regulator (thus reducing costs to the non-home country regulator); and

- focus regulatory resources where they can be most effective, which is typically within their own jurisdictions (thus increasing the benefits provided by external reviews).

In general, we believe that the POB's flexible and proportionate approach outlined in the consultation document is very much consistent with the principles set forth in the above paragraph. Therefore we are supportive of the POB's approach. We believe that the POB's approach properly weights the costs and benefits, and seeks a method of oversight to all third country auditors that takes into account the importance of the issuers that they audit to UK investors. We further believe that the proportionate methodology will suitably allow the POB to modify its approach to specific third country auditors if the significance of the companies under audit from that auditor either increases or decreases.

Our responses to the specific questions follow in an appendix to this letter.

Sincerely

April Mackenzie
Global head governance and public policy

Appendix 1: Responses to Specific Questions

Question 1: Do you agree with the overall approach set out in paragraph 3.2?

Answer: Yes. We agree that the focus of a national audit regulator should be on audits of companies that are significant to investors in that country. In many cases, for example, a company that triggers registration requirements for a third-country auditor will have little significance to UK investors because the listing on the relevant UK-regulated market is secondary to the listing on the home country market, and the risk to UK investors, as a whole, will not be substantial. Therefore, the tailored approach according to the significance of the issuer is sensible.

Question 2: Do you agree with the proposals on "Article 45" auditors set out in paragraph 3.3? If not, what alternative(s) would you propose?

Answer: Generally yes. In particular, we agree with the order of preference set forth in paragraph 3.3 whereby the preferred approach – set forth in the first bulleted sub-paragraph – would be to rely on the home country auditor in the case where a quality assurance review has been carried out in the past three years. We support the POB contacting the home country regulator to request them to review files relevant to the UK, instead of doing its own review.

We also agree with the approach – set forth in the remaining bulleted sub-paragraphs – that emphasizes communication with home country external regulators and professional bodies and the assessment of publically available information, instead of having the AIU initiate its own review.

We do have some concern with the idea (set forth in the fifth bullet point) of asking the network to include a review of a specific relevant audit engagement to the specifications of the POB. This is because the scope and objectives of a network quality assurance review may be different than those of a regulator. While a network's report of a quality assurance review might well be provided to a regulator by the member firm in question upon request, there is similarly no guarantee that it would have been performed to the same scope as the regulator.

Question 3: Do you agree with the proposals for "equivalent" registered TCAs, particularly for US audit firms set out in paragraphs 3.5 to 3.7? If not, what alternative(s) would you propose?

Answer: Yes. As to the nine equivalent third countries that do not intend to monitor UK auditors, we agree with the POB's approach of not applying external monitoring of auditors of issuers located in those countries. As to the USA, we also agree with the POB's approach. In particular, we appreciate that the POB is electing not to simply inspect auditors of US issuers, but will instead first seek to review the findings of the US Public Company Accounting Oversight Board (PCAOB) and discuss with the PCAOB any findings that are particularly relevant to UK investors.

Question 4: Do you agree that the results of external monitoring should be reported to a regulatory committee of the FRC? (paragraph 3.8)

Answer: Yes. It seems appropriate that the results of external monitoring should be reported to an FRC regulatory committee, as long as the confidentiality of the information is maintained. This notion of confidentiality applies regardless of whether the POB conducts the external monitoring or whether the POB has relied upon the report of a third-country regulator that has been provided to the POB under assurances of confidentiality.

In the event that the inspection uncovers audit issues, we believe that the FRC should undertake a graduating scale of actions, depending on the severity of the issue. We suggest that the FRC first try to work with the firm to resolve the issue, which could involve return inspections to identify whether weaknesses have been addressed. In the most severe cases, there could be conditions placed on the firm's registration and even withdrawal of registration, subject to an appropriate appeals process.

Question 5: What charging structure do you consider provides a sensible and fair basis for recovering the costs of external monitoring? (paragraphs 3.9 to 3.11)

Answer: We prefer the second approach. The regime for recovering the costs of external monitoring should not dictate which audit firm is available for appointment by the company. We acknowledge that some costs will arise by virtue of operating overseas. However, we assert that an appropriate balance could be achieved.

We believe that the most appropriate mechanism to achieve this balance is a charge through the annual registration fee plus a charge per year based upon each relevant issuer, so that all registered firms contribute each year towards the overall costs of any inspection program. This would truly include all firms registered with the POB (whether equivalent, transitional or Article 45), not just those firms selected for review in a particular year. In addition, we very much agree that costs for inspection should be calculated on a proportional basis, so that the largest firms with numerous relevant audit clients and largest fees continue to pay substantially more than smaller firms with a few or one client(s).

The first approach – charging each audit firm the costs of the specific review – may prove prohibitively expensive for audit firms in those countries where the hourly rates for conducting an audit are very low compared to the POB's inspection costs. In such a case, it might be difficult to find an audit firm willing to continue to audit the specific issuer in question. Spreading out the costs on a proportional basis amongst all audit firms would eliminate this concern.

Question 6: Do you consider that the information we are proposing to publish, as set out in paragraphs 3.12 and 3.13, is adequate for the needs of investors? If not, what do you propose?

Answer: We generally believe that the information the POB is proposing to publish is adequate.

With respect to the publication of reviews of third country audit firms, we support the approach set forth in paragraph 3.12, which includes an overall annual report on the results of inspections. In general, Grant Thornton supports the publication of results of reviews of independent audit regulators, and we support the AIU's publication of annual reports on each of the major UK firms (defined as those firms that audit over ten entities within the AIU's scope) and a consolidated annual report for those firms that audit ten or fewer such entities. However, we understand that there are relatively few (if any) third country auditors (TCAs) that audit over ten entities, and therefore one general annual report seems appropriate. We believe that such an annual report – and indeed any public report of an audit firm – should not contain client names, and that additional efforts should be taken to ensure that the public cannot determine the name of a particular client whose audit is discussed.

This approach would also be consistent with our belief that published reports should not have the unintended effect of exacerbating audit market concentration by grouping together results of firms in an unwarranted fashion.

With respect to paragraph 3.13, we are also supportive of taking an approach similar to that of the PCAOB, whereby the POB would publish a list of clients of third-country audit firms where the POB is denied access to conduct inspections.

Initially, we expressed concern to the PCAOB about this approach in 2009, on the grounds that the inclusion of audit firms on such a list might wrongly imply that those firms lacked quality or did not cooperate with the PCAOB. However, the PCAOB has published such a list now for a couple of years, and it appears that investors understand it does not mean that the firms on the list lack quality or are uncooperative. Therefore, we would not object to the POB taking a similar approach.

We would request, however, that the POB include cautionary language in connection with the list, stating among other things that the failure to have been inspected:

- does not mean that the audit firm lacks quality; and

- does not reflect that the audit firm is at fault in any way and does not evidence a lack of cooperation, but instead, reflects the inability of the POB and the third country regulator to reach an agreement regarding oversight.

We made a similar request of the PCAOB when it consulted on its list in 2009.

Question 7: Overall, do you consider that these proposals for external monitoring provide the basis for a proportionate and practicable way of meeting the SAD requirements on quality assurance?

Answer: Yes, overall we support the proposals on the grounds stated in the body of our response and in the answers to the prior questions.

Question 8: Do you have any comments on the assessment of costs and benefits in Section 4? We should welcome in particular the assessment of UK investors on the value of benefits that might flow from the two options for external monitoring reviews.

Answer: We agree that the costs of option 1 will substantially exceed the benefits to UK investors, and therefore conclude that it is undesirable for the POB to inspect all 31 audit firms with 43 relevant clients over the three year period.

It is difficult to assess the costs of option 2, as there are no estimates regarding the number of file and firm reviews that would be conducted, but undoubtedly this number would be less than in option 1. We also believe that the benefits to UK investors of option 2 will be substantially similar to those under option 1 because the inspection resources would be directed at the high significance issuers. Therefore, we conclude that the cost-benefit balance of option 2 is more appropriate. However, we also are interested in the assessment of UK investors as to the benefits, as they would be the primary recipients of the benefits of external inspections.