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Our ref **MT/288**
Contact **Mary Tokar**

24 May 2012

Dear Mr Grewe,

FRC Consultation Paper, *Monitoring the Work of Third Country Auditors*

We appreciate the opportunity to provide comments to the Professional Oversight Board (POB) on the FRC Consultation Paper. We have consulted within the KPMG network in respect of this letter, which represents the views of the KPMG network.

We support the POB's proposed approach which generally appears reasonable, pragmatic and scaled, taking into account the significance of the individual issuers. We therefore support the proposals which are, overall, proportionate and practicable. We do have suggestions for the POB's consideration that, in our view, would improve the effectiveness of the POB's approach to fulfilling its statutory inspection mandate.

The appendix to this letter includes our responses to each of the POB's questions. Items that we wish to draw to your attention are highlighted below:

- The POB's proposal to perform off-site reviews of issuer engagements in London may have limited applicability due to local legal and regulatory barriers which may prevent work papers being sent outside the jurisdiction of the local audit firm. In addition, should an off-site review in London be permitted, then we believe that those reviews should be supplemented by discussions with engagement teams both prior to and at the conclusion of the review. We therefore would encourage the POB to develop communication protocols if off-site reviews are pursued. The process in place between the AIU and certain firms in Guernsey and Jersey may be an appropriate template.
- We understand the rationale underlying the POB's assessment of the significance of issuers and countries; however, there should be an opportunity for dialogue for Third Country Auditors if they have additional information that they believe the POB should consider which could impact the POB's initial assessment.



- For the proposed charging structure; we encourage the POB to explore the option of recovering all or part of the inspection costs through a direct levy on the issuer. If this option is not possible, then we would support the retention of the present registration fee and charging the inspection costs to each firm when inspections occur.

If you have any questions about this response then please contact Mary Tokar at +44 (0) 207 694 8871 or David Matthews from KPMG (UK) LLP at +44 (0) 207 311 8572.

Yours sincerely

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Response to specific questions

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

- Yes, we do. We support the POB's objective of scaling its inspection efforts and pursuing an approach of mutual recognition. We would prefer that this be extended to independent audit regulators that are deemed equivalent even if they do not take a mutual reliance approach, as we believe that a mutual reliance approach should be encouraged. We believe that the POB's position appears reasonable given its Statutory Audit Directive obligations under UK law.
- As noted in our cover letter, we believe that there should be an opportunity for dialogue established to allow Third Country Auditors (TCAs) to provide additional information to the POB if the auditor disagrees with the assessment made by the POB. Additionally, it would be helpful if the POB would publish an assessment of the significance of countries currently considered "transitional" for which a determination of equivalence has not yet been made.

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?

We believe that the POB's position is reasonable and pragmatic. However we have the following comments:

- The KPMG network quality reviews include two review programs that are performed annually: a Quality Performance Review Program (QPR), focusing on reviews of individual engagements, and a Risk Compliance Program (RCP), focusing on the control environment of individual member firms. The programs for these reviews are updated annually by KPMG International. A formal report is issued for each of these reviews. The POB has access to information about these review programs via its annual inspection of the UK member firm of the KPMG network. We have not identified any national laws or regulations that preclude a member firm from sharing information with a third-country regulator about their QPR and RCP reports. However, we have not been able to confirm that there are no such restrictions. There is no restriction from a KPMG International policy perspective that precludes a KPMG member firm from sharing their QPR and RCP reports with a home or third-country regulator.
- In contrast with the selection criteria of some regulators which are largely or wholly limited to engagements on issuer clients, the guidelines for KPMG's QPR selection criteria include coverage of each partner over a three-year cycle and over a cross-section of audit and assurance engagement types. Therefore whilst the member firm would seek to accommodate requests from the POB to include a given issuer's audit engagement in the review population, this may not always be possible in any given year as it depends for example on the engagement partner being due for review and also on

the timing of any request from the POB as compared to the timing of the member firm's QPR review.

- The ability to conduct an off-site review of issuer engagements in London may be limited as a number of jurisdictions have indicated there may be local legal or regulatory barriers to such a transfer of work papers. Further, we believe that those reviews should be supplemented by discussions with engagement teams both prior to the review as part of the planning and set-up phase and at the conclusion of the review to verify the factual accuracy of findings. We therefore would encourage the POB to develop protocols if it pursues an off-site review plan. We understand that the AIU is currently engaged in the inspection of certain firms in Guernsey and Jersey where work papers are sent to London and a process has been designed for introductory and closing discussions with the engagement teams which may be an appropriate template.

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?

- The POB's proposed approach in paragraph 3.7 seems reasonable. We suggest that the POB direct requests for additional information to the PCAOB. The POB should contact auditors only if the PCAOB is unable to provide the information.
- We support the intention of the POB to only consider direct inspection if the entity is outside of the PCAOB's inspection scope. For example, the majority of KPMG US LLP's clients listed in the UK are also US registrants and therefore covered by the PCAOB's inspection scope.
- We presume that the POB would carry out an assessment of significance of the remaining issuers audited by the US firms registered in the UK, similar to that proposed for issuers audited by other TCA firms, and thereby potentially limit direct inspection further.

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

We agree with the proposal.

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)

- The POB's obligation to inspect third-country auditors is a direct consequence of third-country issuers obtaining a UK listing. Therefore we believe that it would be appropriate for the POB to recover the TCA inspection costs to the greatest extent possible via an issuer levy.

- If recovery via a levy to issuers is not possible then we support the retention of the current registration fee and charging costs of an inspection to each firm as and when inspections occur.

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?

The proposals for publication are, in general, appropriate, however:

- The POB has not provided any detail of the information it intends to publish; therefore, our ability to comment on the adequacy of information to be published, and whether or not there are any possible conflicts with privacy laws in the third countries involved, is limited. The privacy issues may be more pressing in cases in which there is a single UK issuer audited by an inspected firm. If the information will be basic information identifying firms where inspections have taken place then we have not identified any privacy restrictions.
- The reasons for any denial of access to the POB should be presented clearly in the POB publication.
- In particular, where this denial is due to country laws or regulations rather than refusal of access by any one firm, it should be specified.
- The publication could also present the POB's assessment of significance for each country and issuer.

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? (After paragraph 3.13)

We support the POB's proposals as pragmatic and scaled and as taking into account consultations with affected registered firms and their international networks. Therefore, subject to our comments presented as responses to the other questions, we agree that the proposals are, overall, proportionate and practicable.

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.

- As stated in our response to Question 5, our preference would be for the POB to recover costs through a listing levy on issuers; but from the options given, we prefer specific billing of each inspection as and when it occurs.

- The balance of costs and benefits will depend on transparent and robust assessment of country and issuer significance and the appropriate reliance on other inspection sources, as proposed by the POB, whenever the significance is other than high.
- KPMG therefore endorses “Option 2” to apply the tailored approach set out in paragraph 3.3 of the POB Consultation Document in order for the POB to meet its Statutory Audit Directive obligations.