

**Transparency of Firms that Audit
Public Companies
Consultation Report**

Comment Letters



**TECHNICAL COMMITTEE
OF THE
INTERNATIONAL ORGANIZATION OF SECURITIES COMMISSIONS**

OR07/10

OCTOBER 2010

IOSCO Consulting Paper
Transparency of Firms that Audit Public Companies
List of Comment Letters Received

No.	Respondent Organization
1.	Basel Committee on Banking Supervision
2.	Canadian Public Accountability Board
3.	The Compagnie Nationale des Commissaires aux Comptes (CNCC)
4.	Conway, Robert – Individual CPA
5.	Deloitte Touche Tohmatsu
6.	Dubai Financial Services Authority
7.	European Group of International Accounting Networks and Associations
8.	EUMEDION Corporate Governance Forum
9.	Ernst & Young Global Limited
10.	FAR SRS (The Institute for the Accountancy Profession in Sweden)
11.	Federation of European Accountants
12.	Financial Reporting Council
13.	Grant Thornton International Ltd.
14.	The Institute of Chartered Accountants of Scotland (Audit and Assurance Committee)
15.	Instituto De Censores Jurados De Cuentas De Espana
16.	Institut der Wirtschaftsprufer
17.	International Federation of Accountants
18.	KPMG International
19.	The Nordic Federation of Public Accountants
20.	PricewaterhouseCoopers LLP
21.	SEC Thailand



BASEL COMMITTEE ON BANKING SUPERVISION

BANK FOR INTERNATIONAL SETTLEMENTS

Chairman

Via email: AuditorTransparency@iosco.org

Mr Greg Tanzer
Secretary General
IOSCO General Secretariat
Calle Oquendo 12
28006 Madrid
Spain

14 January 2010

Public Comment on the consultation report "Transparency of Firms that Audit Public Companies"

Dear Mr Tanzer

The Basel Committee welcomes the opportunity to provide a general comment on IOSCO's consultation report *Transparency of Firms that Audit Public Companies*.

The Committee has a strong interest in high-quality audits of published financial statements. This is because high-quality audits of banks complement supervisory processes and increase supervisory efficiency. This notion has been firmly established in our paper, *External audit quality and banking supervision*, which was published in December 2008.

The Committee's *External audit* paper recognises that the vast majority of banking assets are audited by the four largest globally active accounting firms. It notes "*The large globally active firms do not provide sufficient public information about how the firms are managed on a global basis, how audit quality is assured at the global level, or about their world-wide overall financial condition and profitability.*"¹

Understanding how globally active accounting firms are governed is necessary to ensure that there is sufficient audit quality maintained in these organisations' that audit banks.

The Committee, therefore, welcome your consultative report on transparency of firms that audit public companies, and looks forward to seeing the results of the consultation. We believe it would also be mutually beneficial for the audit sub-groups of the Basel Committee and IOSCO to meet and discuss the results of the consultation and other audit quality issues of common interest.

¹ *External audit quality and banking supervision*, page 14. This report is available at www.bis.org/publ/bcbs146.htm.

This letter has been prepared by the Committee's Accounting Task Force, chaired by Mrs Sylvie Mathérat, Director of the Banque de France, and has been approved by the Committee. If you have any questions regarding this letter, please feel free to contact Mrs Mathérat (+33 1 4292 6579), Marc Pickeur who chairs the Audit Subgroup of the Accounting Task Force (+32 2 220 5253) or Rob Sharma at the Basel Committee Secretariat (+41 61 280 8007).

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Nout Wellink', with a large initial 'N' and a long, flowing horizontal stroke.

Nout Wellink



CANADIAN PUBLIC ACCOUNTABILITY BOARD
CONSEIL CANADIEN SUR LA REDDITION DE COMPTES

150 York Street, Suite 200, Box 90, Toronto, Ontario M5H 3S5
Tel 416.913.8260 Fax 416.850.9235 www.cpab-ccrc.ca

January 13, 2010

Mr. Greg Tanzer
Secretary General
IOSCO General Secretariat
Calle Oquendo 12
28006 Madrid
Spain

Dear Mr. Tanzer:

**Re: Public Comment on the Transparency of Firms that Audit Public Companies:
Consultation Report**

The Canadian Public Accountability Board (CPAB) is pleased to comment on the consultation report “Transparency of Firms that Audit Public Companies”. CPAB is very supportive of the work being performed by the International Organization of Securities Commissions (IOSCO) to explore ways to improve audit quality and we compliment IOSCO on the high quality of the consultation report. In light of the challenging economic climate and audit fee pressures that many firms are currently facing it is all the more important that firms maintain a focus on audit quality.

Audit Quality

Audit quality is subjective in nature and in our experience is best evaluated based on key drivers/indicators of audit quality, many of which have been highlighted in the consultation report. However, caution has to be exercised when evaluating data obtained from firms to ensure there is consistency when comparing firms and to ensure that data is being interpreted appropriately. For example, if a firm is obtaining new public company audit clients this may be more due to the firm’s competitive pricing rather than superior audit quality.

Increased competition amongst firms based on audit quality is a desirable goal and we believe more research and analysis is required on the best ways to achieve this. We also note that the International Auditing and Assurance Standards Board (IAASB) has an Audit Quality project proposal scheduled for June 2010. In our view, it makes sense for international bodies such as IAASB, IOSCO and IFIAR (International Forum of Independent Audit Regulators) to have a coordinated approach to develop ways to improve audit quality.

Transparency of Audit Firms

In discussions on transparency of audit firms it is important to focus on the key objectives of increased transparency. A key objective should be to drive positive changes in behaviour such that audit quality is improved. However, if firm disclosures are too high level there is a risk of these becoming boiler-plate with very little to distinguish one firm from another in areas such as audit quality. It is important the appropriate disclosures are developed so that audit quality may be meaningfully compared and improved. With increased globalization of the major accounting firms it is especially critical for regulators to understand global networks and how quality control systems are implemented, maintained and monitored.

CPAB has an effective working relationship with the firms it inspects and receives a high level of cooperation from the firms. Increased transparency should not negatively impact firm cooperation with audit regulators and firm responsiveness to audit regulator findings and recommendations to improve audit quality. In certain areas it may be more effective for audit regulators to “monitor” firms and related risks as opposed to making public disclosure.

In conclusion we reiterate our support for the work being performed on audit quality and audit firm transparency and we appreciate the opportunity to provide input on the consultation report.

We would be pleased to discuss any of the above comments.

Yours very truly,

A handwritten signature in dark ink, appearing to read 'Brian Hunt'.

Brian Hunt, FCA
Chief Executive Officer



LE PRÉSIDENT

Mr. Greg Tanzer
Secretary General
IOSCO General Secretariat
Calle Oquendo 12
28006 Madrid
Spain

auditorcommunications@iosco.org

27 January 2010


Dear Mr. Tanzer,

Re: Comments on the IOSCO consultation report dealing with transparency of audit firms auditing public interest entities.

The Compagnie Nationale des Commissaires aux Comptes (CNCC) is pleased to provide you below with its comments on IOSCO's consultation on transparency of audit firms auditing public interest entities.

If you have any further questions about our views on this consultation, please do not hesitate to contact us.

Yours sincerely,



Claude Cazes
President of CNCC

Transparency of audit firms auditing public interest entities

Reply to the IOSCO consultation report

The Compagnie nationale des commissaires aux comptes (CNCC) welcomes the opportunity to provide its comments related to the IOSCO consultation report dealing with the transparency of audit firms auditing public interest entities.

This response includes, as an introduction, general comments on the consultation on the one hand, and the responses to the questions mentioned in the consultation report on the other.

I – Introduction

As an introduction, the CNCC specifies that to our knowledge, there is no cause-and - effect relationship whatsoever between the transparency of audit firms and audit quality. Moreover, if transparency seems to be a significant element to the credibility of audit firms, according to the CNCC, the consultation seems to deal with transparency both through the supervisory authorities and through the public, without distinguishing those various users whose needs are obviously not the same. The CNCC considers that it is essential that information related to transparency disclosed by the firms is approved by the supervisory authorities, to make sure that the various information disclosed by the various firms can be compared.

II – Answers to the various questions raised by the consultation:

1. Is a definition of audit quality necessary to evaluate audit quality or can audit quality be evaluated from an understanding of the attributes, behaviors, and indicators of audit quality?

1 – The CNCC recommends waiting for the results of the IAASB studies currently held on the project dealing with the issue of the “expectation gap” in terms of audit quality.

2. In addition to competence and industry expertise of the audit personnel, firm culture that promotes audit quality, firm-wide quality control systems, and auditor oversight, are there other examples of attributes, behaviors, and indicators of audit quality that should be considered?

2 – The CNCC considers that the principles mentioned in the consultation report should not refer only to competence, firm culture, quality control and auditor oversight. One could also raise the principles that are within the IFAC Code of Ethics and in the ISQC1 standard, such as : integrity, objectivity, confidentiality, due diligence, professionalism, as well as the components which are enshrined in the policies and the procedures of the quality control system, according to ISQC1 : the role of those in charge of quality control within the firm, the rules of ethics, follow-up of the client acceptance, human resources, achievement of the assignment, follow-up of the quality control system. Equally, the CNCC would like to put forward the fact that audit quality relies mainly on the quality of human resources, hence the importance of initial training that develops general knowledge and open-mindedness, essential qualities for audit quality, that would not be developed via continuing education.

3. Are there other areas of governance for which additional transparency should be considered?

3 – The CNCC considers that the publication of the annual report on transparency, as stated by the Article 40 of the Directive for the statutory auditors and audit firms which attest the accounts of listed entities, is sufficient; in addition, the requirement to issue a transparency report is recent, and the member states which have implemented this process have no background on the possible outcomes entailed by the publication of these reports.

4. Would the proposed disclosures mentioned above be useful in improving audit quality and availability and delivery of audit services to public companies?

4 – The CNCC considers that the information to be given within the transparency report is sufficient.

5. Could other limitations arise if such disclosures were required?

5 - It is important to allow a possibility to waive any information publication requirement that could create an immediate and significant threat related to the security of an individual.

6. Can audit quality indicators provide objective information when evaluating a firm's audit quality? If so, do the ones identified in this report accomplish that goal?

6 – The CNCC believes that it is difficult to identify audit quality indicators that would take into account all the fundamental principles to be considered to assess audit quality. Moreover, the CNCC considers that the indicators proposed are not appropriate, because they have been defined subjectively, and moreover, these indicators could be interpreted differently and entail negative effects thereby playing against the goal to be achieved through transparency.

7. In addition to the indicators identified in this report, are there any other audit quality indicators that should be considered for disclosure? Would disclosure of the audit quality indicators described above be helpful in evaluating audit quality?

7 – As mentioned in the response to question 6, the CNCC does not favour the identification of audit quality indicators.

8. In addition to the benefits or limitations identified in this report, are there any other benefits or limitations about disclosing audit quality indicators that need to be considered?

8 – As mentioned in the response to question 6, the CNCC considers that the publication of audit quality indicators could entail negative effects playing against the goal to achieve.

9. Can audited financial statements of audit firms provide useful or objective information regarding audit quality? If so, how?

9 – The CNCC considers that the question is not applicable in France, because French audit firms disclose their financial statements. However, the CNCC would like to point out that analysing the financial statements could lead to various interpretations and have negative effects (for example, a profit could let people think that due diligence is not duly complied with...)

10. If disclosure to the public or regulators of an audit firm's own audited financial statements is warranted, who should audit the auditors? Are firms other than the Big Four equipped to audit the Big Four? If not, does having the Big Four firms audit each other raise concerns? If so, how could any such concerns be addressed?

10 – The CNCC considers that the question is not applicable in France, because it is mandatory for the French audit firms to have a statutory auditor.

11. Can disclosing certain financial information instead of audited financial statements achieve the same objective of improving audit quality and the availability and delivery of audit services? If so, what financial information should be disclosed?

11 – The CNCC considers that the question is not applicable in France, because audit firms disclose their financial statements.

12. Are there other parameters that should be considered?

12 – The CNCC considers that the parameters proposed are sufficient.

13. Should certain disclosures not be publicly available and if so, what criteria should be considered when determining what disclosures should be publicly available?

13 – The CNCC considers that, at this stage, the transparency report is sufficient as it is publicly available.

14. Should certain disclosures be made at the network, firm, and/or, engagement level?

14 – The CNCC suggests sticking to the transparency report, which is disclosed by each professional structure, even if it includes a description of the network. It is important to point out that the supervisory authority approves the content of the report.

15. Should there be different disclosure requirements for large, mid-size, and small audit firms?

15 – The CNCC considers that one should stick to the rules applicable to the transparency report, which is compulsory in France for the firms conducting a statutory audit of publicly held entities having securities quoted on a regulated market, whatever the size of the firms.

16. Should the disclosures be mandatory and if so, should they be subject to regulatory oversight? Would a similar impact to the markets occur if the disclosures were encouraged instead of being mandatory? Should consideration be given to a framework of audit quality and allow for flexibility in the types of disclosures?

16 – The CNCC considers that it is preferable that the disclosures be mandatory, and approved by the supervisory authority.

17. Would transparency of audit firms improve audit quality and the availability and delivery of audit services? What negative effects, including costs, of increased transparency should regulators consider?

17 – As mentioned in the introduction, the CNCC considers that, as far as it knows, there is no cause-and-effect relationship between transparency and audit quality, but on the other hand, more transparency would entail negative effects if the information disclosed by each firm is not comparable.

18. Would investors have increased confidence in financial reporting as a result of increased audit firm transparency?

18 – The CNCC is not in a position to respond on behalf of investors, although it considers that the disclosure of transparency reports may bring more confidence regarding the auditors of the audited firm and, consequently, regarding the quality of the financial reporting of the audited entity.

19. Are there significant benefits to investors of increased audit firm transparency, since they invest in companies and not audit firms?

19 – Please refer to question 18

20. Should regulators consider areas outside of audit firms' governance, audit quality indicators, and financial statements for potential disclosures?

20 – The CNCC suggests sticking to the transparency report.

International Organization of Securities Commissions

Response to Request for Public Comment on
Transparency of Firms that Audit Public Companies

November 25, 2009

My name is Robert Conway. I am a licensed Certified Public Accountant in the United States and a retired Big Four audit partner. I am also an employee of the Public Company Accounting Oversight Board (“PCAOB” or “the Board”). The views I express herein are my own and do not necessarily reflect those of the Board, Board Members, or other members of the PCAOB staff. Prior to joining the PCAOB in 2005, I had a 26+ year career with one of the Big Four public accounting firms, including 17+ years as an audit partner.

I am also the author (identified at the time only as the “Anonymous Retired Audit Partner”) of the recommendation¹ to the United States Treasury Department’s Advisory Committee on the Auditing Profession (“ACAP”) that audit firms be required to publicly report certain operational metrics which I referred to as “Audit Quality Drivers.” The thinking behind this recommendation was that the operational metrics of competing audit firms would be of interest to the purchasers of audit services and competitive forces would drive audit firm leaders to improve their operational metrics in a direction conducive to improving audit quality. After all, what audit firm leader would want to be in last place when the metrics are published and what audit committee would desire to engage an audit firm with the least desirable blend of operational metrics? The six metrics I proposed in my ACAP recommendation and the desired direction of improvement are summarized below:

<u>Audit Quality Driver / Metric</u>		<u>Desired Direction of Improvement</u>
Years experience after CPA licensing	>>>	More experienced professionals
Percentage staff turnover during year	>>>	Better continuity year over year
Chargeable hours per professional	>>>	More reasonable staff workloads
Chargeable hours managed per partner	>>>	More reasonable partner workloads
Ratio of audit staff to partners	>>>	Better supervision
Training hours per professional	>>>	Increasing technical excellence

My recommendation to ACAP has been widely regarded as having provided the impetus for ACAP’s recommendation that the PCAOB determine the feasibility of developing key indicators of audit quality and the effectiveness of requiring audit firms to publicly disclose these indicators. Damon Silvers, Chairman of ACAP’s Subcommittee on Concentration and Competition noted during the PCAOB’s October 22, 2008 Standing Advisory Group discussion on audit quality metrics, “I could say that our [ACAP] subcommittee came up with this recommendation out of the fullness of our imaginations. It really is not so. It came from a comment letter that we received from a retired audit firm partner who chose to remain anonymous -- and it is really a tribute to the quality of that letter that it drove this recommendation.”² While my recommendation focused on input measures of audit

¹ See <http://comments.treas.gov/files/AuditQualityRecommendation.doc> for my complete recommendation to ACAP. The disclaimer in the first paragraph above about the views expressed herein also applies to my ACAP recommendation.

² See webcast at http://www.pcaob.org/News_and_Events/Webcasts.aspx#57 at 2:02:45.

quality, the ACAP discussion expanded the recommendation, asking the PCAOB to consider both input and output indicators.³

In the corporate world, we know that the pressures on business leaders to produce near term profits are enormous. The leaders of the public accounting firms are subject to these same pressures – and perhaps even more so – because the cash distributions to the audit partners are typically based on current year profitability. Granted, one must be mindful that poor audit quality can lead to costly litigation and higher malpractice premiums – but those costs generally manifest themselves years later after existing firm leadership has moved on. The profit motive, left unchecked, is largely responsible for the high leverage, high workload, high turnover, and low experience level business model the audit firms continue to follow. The effects of that business model are further compounded by the quadropoly situation that exists today where four audit firms dominate the audit services market globally. Increased transparency would create the opportunity for the market place to influence the large firms to strike a better balance between fees, profitability, and operational metrics – so that the audit firms operate in an environment which is more conducive to reasonable workloads, lower staff turnover, better supervision and review, and more experienced and knowledgeable professionals – all of which collectively should improve audit quality.

Observation A: Transparency and Audit Firm Competition for the Most Talented People

There is an important group of people, in addition to the purchasers of audit services, which will be empowered by the transparent reporting of the audit quality drivers. I am talking about the accounting graduates seeking employment in the auditing profession. The best graduates are not likely to decide to go to work for the auditing firm with the highest turnover, the heaviest workloads, the least amount of supervision, and the lowest investment in training. The audit firms will need to compete for the best recruits by being competitive on the operational metrics of interest to prospective employees.⁴ In addition, each firm's ability to retain existing employees and stem the loss of employees to competing firms will depend, in part, on each firm's ability to be competitive on the operational metrics. It is not unreasonable to expect that such competition will drive audit firm leadership to improve the operational metrics in a direction that will be conducive to improving audit quality.

The line audit partner (the audit partner who signs the audit opinion) is also an important stakeholder in the transparency of operational metrics. The line audit partner bears significant career risk from litigation and enforcement actions that may result from deficient auditing. This risk can lead to the loss of the line audit partner's CPA license and livelihood. While I believe the line audit partners work very hard to manage this risk, the high leverage, high workload, low experience level, and high turnover business model are not conducive to mitigating this risk. As a consequence, I believe the line audit partners would be particularly supportive of the transparent disclosure of the operational metrics suggested on page 1. Competition should drive the operational metrics in a direction which will better mitigate line audit partner career risk as compared to the existing large firm business model.

³ See Chapter VIII, page 14 of the ACAP report at <http://www.treas.gov/offices/domestic-finance/acap/docs/final-report.pdf>.

⁴ This observation was part of a second recommendation I made to ACAP. See <http://comments.treas.gov/files/RetiredAuditPartneronTransparencyandAuditQualityMetrics.doc>. The disclaimer in the first paragraph of this paper about the views expressed herein also applies to my second ACAP recommendation.

As IOSCO evaluates public comments that it may receive from audit firm leadership, I encourage IOSCO to bear in mind that the views of the large firm leaders may differ from the line audit partners -- because the large audit firm leaders are not directly threatened by the type of personal career risks which are shouldered by the line audit partners.

Observation B: Input Versus Output Measures – Not an “All or Nothing” Debate

I applaud IOSCO for publishing its consultation report on “Transparency of Firms that Audit Public Companies” and raising the discussion of this important issue to a global level. It is good that your discussion considers both input and output metrics. However, I’d like to emphasize that I do not believe that the discussion of input versus output measures needs to be an all or nothing debate. I think there are two very feasible options: 1) requiring the transparent reporting of only input metrics or 2) requiring the transparent reporting of both input and output metrics. The use of input metrics has the advantage of being much more objectively verifiable while the use of various output measures may be subject to misinterpretation and the reality that there may be a lengthy time lag before poor audit quality manifests itself in the output measures.

The input metrics I have proposed do not directly drive “other important factors” impacting audit quality such as professional skepticism, technical competence, industry expertise, and the fortitude to tell an important client “no” when warranted. However, I believe it is intuitive that the input metrics can have an indirect favorable impact on many of these “other important factors.” For instance, the judgment of an audit partner and audit manager can be clouded if they are swamped with work such that they are late to identify and elevate an issue to management. No one likes last minute surprises in a world where earnings release dates are perceived as dates that can not be missed. Late detection of issues can cloud partner fortitude to tell a client “no” because of the backlash that may result from the client who asks “Why am I only hearing about this now – just before the earnings release?”

It is intuitively obvious that any complex undertaking by a team of people requires:

- A reasonable allowance of time for each team member to do a good job,
- Good team member continuity throughout the duration of the project,
- Team members with appropriate experience levels,
- Sufficient training relevant to the tasks at hand, and
- An appropriate amount of supervision and review.

These are fundamentals elements that must exist in appropriate quantities to enable an audit team to function at a high level. Whether a suitable list of output metrics can be formulated or not, I strongly encourage IOSCO to, at a minimum, recommend the use of input measures to improve audit firm transparency and audit quality.

Observation C: The Circumstances Warrant Transparency

Much has been said in the financial press about the dangers of having only four large audit firms. There has been criticism about the lack of competition, escalating fees, and deteriorating service due to the so-called “quadropoly.” There is also concern about “What happens if one of the Big Four should go out of business?”

Historically, governments have recognized the need to provide increased oversight and regulation in monopoly or oligopoly situations. In that context, imposing increased transparency from the Big Four firms would be a very modest requirement – well within the range of traditional government regulation and oversight. The upside of transparent reporting is that competitive forces can drive improvements in the large audit firm business model. This means that service levels and audit quality will improve, benefiting the consumers of audit services. It also means that the probability of audit failures will be reduced – thereby enhancing the long term sustainability of each firm.

Don Nicolaisen, ACAP co-chairman, former Chief Accountant at the SEC, and a retired audit partner from a Big Four firm, made the following observation during the ACAP deliberations on the importance of improving audit firm transparency: “...the firms compete primarily on the basis of cost. And that’s been the history of the profession. And it has been disastrous for investors and for the firms.”⁵

Observation D: Responding to Concerns About Increased Litigation

Concerns have been raised by some that the disclosure of operational metrics will only increase an audit firm’s exposure to litigation. Granted, there is risk that an attorney will pursue litigation against an audit firm on the basis that the operational metrics for a failed audit were materially different from the firm-wide averages. That very well might happen. But shouldn’t the audit firm have mitigating or compensating procedures that are activated when the operating metrics for an office or an individual audit engagement imply that experience levels are low, staff or partner workloads are excessive, turnover is excessive, supervision is spread thin, or training is lacking? It is conceivable to me that once transparent disclosures of operational metrics are required, the next logical step will be for the audit firms to internally define “**safe zones of operation**” and compensating procedures that need to be activated when audit operations move outside the “safe zone of operation.” An example of a possible compensating procedure would be the expansion of the scope of the second partner review of the audit work papers. This would clearly be a positive development – as it would lead to a higher level of quality control than exists today.

⁵ Quote from Don Nicolaisen is from the minutes of the April 1, 2008 meeting of the Advisory Committee on the Auditing Profession. See <http://www.treas.gov/offices/domestic-finance/acap/agendas/minutes-04-01-08.pdf>, page 59.

Observation E: Responding to Concerns About Unintended Consequences

In response to those who fear that transparency will bring with it adverse unintended consequences – I offer the following recommendation. The transparent reporting by the audit firms should be made in a two year comparative format with discussion and analysis of the results and trends provided by the audit firm’s leadership. This will enable audit firm leadership to explain anything that may be subject to misinterpretation – much in the way public companies explain how their operating results reflect the effects of their business strategies and market conditions. To assure comparability of information from firm to firm, it will be important that the local overseer of the auditing profession provide guidance and review of the manner in which transparent information is compiled and reported. In the early implementation of transparent reporting, I envision that the local regulator will need to work closely with the audit firms to resolve computational issues that are likely to arise before any public reporting commences. In time, transparent reporting will progress to a more routine process with well defined guidelines and reporting deadlines – with periodic regulatory review of the accuracy of the transparency disclosures.

I also foresee a need to develop standardized cautionary language to accompany the transparency disclosures that draws attention to the inherent difficulties associated with measuring audit quality – recognizing that many key elements of audit quality (such as judgment, fortitude, and technical competence) are difficult to measure. Despite such caveats, I firmly believe that the benefits of increased transparency far outweigh any inherent limitations associated with such disclosures.

Observation F: A Point of Clarification on the Outcomes of Academic Studies

The IOSCO Consultation Report (under “*Negative Consequences*” on page 17) states:

“Academic studies show a lack of conclusive evidence about whether many input-based factors have a direct positive relationship with audit quality. Industry experience of the engagement team and professional competence, however, may be two factors that appear to more consistently support an association with improved audit quality, although these factors are difficult to measure in an objective manner.”

This statement in the IOSCO Consultation Report is followed by a footnote reference to supporting material that in turn makes a footnote reference to a public comment document submitted to ACAP by the University of Tennessee Corporate Governance Center (“UTC GC”). The UTC GC document more fully states:

“Moreover, although many of the suggested input-based measures seem intuitively likely to improve audit quality, we are aware of no empirical evidence to suggest that these metrics lead to better audit quality (probably because audit firms typically do not provide such data to academics; see our other comments regarding the issue of data accessibility under Human Capital).”⁶

Thus, “the lack of conclusive evidence about whether many input factors have a direct positive relationship with audit quality” may be due to the fact that the larger audit firms have not given

⁶ See page 10 of the May 15, 2008 public submission to ACAP by the University of Tennessee Corporate Governance Center which can be found at: <http://comments.treas.gov/files/ACAPCommentLetterMay152008.pdf> .

academia access to the data needed to determine if a direct positive relationship exists. The final ACAP report similarly noted: “The Committee also heard from several witnesses regarding the unavailability of data relating to auditing practice and the impact this lack of data has on research and potentially on the profession’s sustainability.”⁷ The lack of access to such information does not mean input indicators should be ignored. To the contrary, the UTCGC notes, “many of the suggested input-based measures [discussed by ACAP] seem intuitively likely to improve audit quality...”

Lynn Turner, ACAP member and former Chief Accountant at the United States Securities and Exchange Commission has commented as follows:

“...people already manage a lot by the numbers. I don’t know why people are worried about putting numbers out there that people manage to. Each of the firms manage to numbers anyway. They manage to a budget number for revenue each year, labor costs as a percent of revenues, partner contribution [to profit], rate per hour, [and the] number of billable hours that each partner is responsible for. We’ve already got those out there and they are already managing to them. So the fact that someone would say well, let’s actually manage to something that relates to audit quality only seems to be common sense and not rocket science.”⁸

Responding to Specific Questions for Public Comment in the IOSCO Report

In the pages that follow, I have responded to selected questions raised for public comment in the IOSCO Consultation Report.

Concluding Remarks

In closing, I would like to reiterate my appreciation for IOSCO’s interest in the “Transparency of Firms that Audit Public Companies.” I firmly believe this is a worthwhile endeavor. I hope you find my commentary helpful during the course of your deliberations.

Sincerely,



Robert A. Conway, CPA
Irvine, California
United States
RetiredAuditPartnerACAP@live.com

⁷ See Chapter V, page 23 of the ACAP report at <http://www.treas.gov/offices/domestic-finance/acap/docs/final-report.pdf> .

⁸ Quote from Lynn Turner is from the PCAOB’s October 22, 2008 Standing Advisory Group discussion on audit quality metrics. See webcast at http://www.pcaob.org/News_and_Events/Webcasts.aspx#57 at 2:36:45.

Response to Selected Questions Posed by IOSCO in the Consultation Report

Below are my personal views with respect to selected “Requests for Consultation” posed by IOSCO in the IOSCO Consultation Report titled, “Transparency of Firms that Audit Public Companies.”

Request

Number Question / Response

- 1 Is a definition of audit quality necessary to evaluate audit quality or can audit quality be evaluated from an understanding of the attributes, behaviors, and indicators of audit quality?

A definition of audit quality would be useful for sake of discussion. But I think it is more important to identify and understand the many variables that impact audit quality. The primary variables that come to mind are:

- a. Professional skepticism;*
- b. Technical competence;*
- c. Compliance with a technically sound audit methodology;*
- d. Independence;*
- e. The fortitude to take a stand on auditing and accounting issues when warranted;*
- f. An active audit committee that fosters a “get it right” tone and makes it clear to the audit team and management that the audit team reports first and foremost to the audit committee, not management;*
- g. Proper audit firm “Tone at the Top”;*
- h. An environment conducive to seeking consultation when appropriate;*
- i. A performance measurement systems that reinforces audit quality, “getting it right”, and consultation;*
- j. A vibrant risk management function;*
- k. A vibrant quality control / internal inspection program; and*
- l. An audit firm business model which provides for:*
 - o Suitably experienced professionals (years experience after CPA licensing),*
 - o Professionals who are suitably knowledgeable about the audit firm’s methodology and the company being audited (percentage staff turnover),*
 - o Reasonable staff workloads (chargeable hours per professional)*
 - o Reasonable partner workloads (chargeable hours managed per partner),*
 - o Appropriate supervision and review (ratio of audit staff to partners), and*
 - o Sufficient professional training on new developments in auditing, accounting, and finance (training hours per professional).*

My personal view based on my large firm audit experience in the United States is that items “a” through “k” receive considerable attention, both by the firms themselves and from external sources. Although the business model (item “l”) is listed last above, my

Request
Number

Question / Response

personal view is that without a business model which is conducive to doing good work, items “a” through “k” all will suffer in one form or another.

The items listed in parentheses in item “l” correspond to the operational metrics listed on page 1 of this paper. It is these metrics which I have recommended for public reporting by the audit firms. Competition among audit firms for clients and new employees will drive the audit firms to improve their operational metrics in a direction which can improve audit quality.

The public reporting of the operational metrics is not a silver bullet or a cure-all to prevent all audit failures. Nonetheless, I believe it represents a significant opportunity to drive audit quality – with the added benefit of potentially enhancing the auditing profession’s ability to attract and retain the best professionals.

- 2 In addition to competence and industry expertise of the audit personnel, firm culture that promotes audit quality, firm-wide quality control systems, and auditor oversight, are there other examples of attributes, behaviors, and indicators of audit quality that should be considered?

Professional skepticism and the fortitude to tell an important client “no” when warranted are also important determinants of audit quality. A strong, independent, and active audit committee, with a “let’s get it right” attitude can foster auditor fortitude to “do the right thing” -- so that the auditor does not feel that he or she is placing the auditor–client relationship at risk by saying “no” to management.

- 4 Would the proposed disclosures mentioned above [i.e. governance, quality control systems, HR policies, ethics, and independence] be useful in improving audit quality and availability and delivery of audit services to public companies?

Each of the large US audit firms distribute information to the audit committees of their New York Stock Exchange traded public company audit clients describing their internal quality control processes. This information is distributed pursuant to the requirements of the New York Stock Exchange Listing Standards. This information includes, among other things, the audit firm’s internal quality control procedures and any material issues raised by the most recent internal quality-control review, or peer review of the firm or by any inquiry or investigation by governmental or professional authorities within the preceding five years. While I believe this information is very useful, the utility of this information would be greatly enhanced if it were to include the types of metrics I listed on page 1 of this paper as well as other relevant output measures.

Request
Number

Question / Response

- 6 Can audit quality indicators provide objective information when evaluating a firm's audit quality? If so, do the ones identified in this report accomplish that goal?

I believe the audit quality indicators described in the IOSCO Consultation Report will provide objective information that will enhance the understanding by market participants of each audit firm's commitment to quality (market participants being defined as the purchasers of audit services as well as prospective employees of the audit firms).

- 8 In addition to the benefits or limitations identified in this report, are there any other benefits or limitations about disclosing audit quality indicators that need to be considered?

In my "Observation A" on page 2 of this letter, I described how prospective employees will benefit from knowing the audit quality indicators of competing firms – and how that information will motivate the audit firms to improve their audit quality metrics.

In my "Observation D" on page 4 of this letter, I described how publication of the metrics may motivate the audit firms to define "safe zones of operation" and additional review requirements that the audit firms might decide to put in place in the event operations move outside the "safe zone of operation." The audit firms would be motivated to do this to discourage litigation based audit quality metric outliers. This could result in a quality control improvement beyond those currently in place.

In my "Observation E" on page 5 of this letter, I outlined my response to those who express concern about the prospect of unintended consequences. I believe such concerns have been overstated and can be satisfactorily addressed by providing each firm the opportunity to provide management's discussion and analysis of its own operating metrics.

In my "Observation F" on page 5 of this letter, I responded to a concern raised on page 17 of the IOSCO report that "Academic studies show a lack of conclusive evidence about whether many input-based factors have a direct positive relationship with audit quality." I noted in "Observation F" that the ultimate source document for this quote more fully explains that the lack of conclusive evidence is "probably because audit firms typically do not provide such data to academics" so they could conduct a suitable analysis. The absence of empirical evidence should not impede progress on the use of audit quality drivers as many have noted that the input based measures seem intuitively likely to improve audit quality.

Request
Number

Question / Response

- 9 Can audited financial statements of audit firms provide useful or objective information regarding audit quality? If so, how?
- I do not believe that public distribution of audited financial statements of the audit firms is warranted or beneficial. I do believe, however, that such information should be routinely provided to regulatory agencies with oversight responsibility for the audit firms.*
- 14 Should certain disclosures be made at the network, firm, and/or engagement level?
- I would favor audit quality driver disclosure at both the firm and regional levels. I would leave requests for disclosure at the engagement level up to the discretion of each audit committee.*
- 15 Should there be different disclosure requirements for large, mid-size, and small audit firms?
- See # 16 below.*
- 16 Should the disclosure be mandatory and if so, should they be subject to regulatory oversight?
- I believe the disclosures should be mandatory for the large audit firms because of the high percentage of total market capitalization audited by those firms – and yes, such disclosures should be subject to regulatory oversight.*
- I believe the disclosures should be optional for mid-size and small audit firms. However, those mid-size and small audit firms that opt to make such disclosures should be required to comply fully with all disclosure requirements and those disclosures should be subject to regulatory oversight.*
- 17 Would transparency of audit firms improve audit quality and the availability and delivery of audit services? What negative effects, including costs, of increased transparency should regulators consider?
- When buying products and services, consumers and corporations typically have ample information to consider during the procurement process. Such information may include consumer reports, product performance specifications, consumer satisfaction surveys, on-time arrival statistics and the like. When it comes to procuring audit services, there is very little information to aid in decision making beyond personal chemistry, the resumes of the engagement team, service level commitments, and references. The audit quality drivers described on page 1 of this letter can provide useful information to the consumers of audit services to assist them in their decision-making process. More importantly, competitive forces can be expected to motivate the leaders of each firm to manage their businesses in the direction of improving the audit*

Request
Number

Question / Response

quality drivers – as no large firm leader will want to be in last place when the metrics are published and it is unlikely that audit committees will want to engage an audit firm with audit quality drivers that compare unfavorably to the audit firm’s competitors. Additionally, the large firms will need to compete for the best talent with full transparency to the working environment provided to its professionals. I would anticipate that overall, we would see improvements to the audit firm basic business model in the form of reduced turnover, higher experience levels, better supervision and review, and increased commitment to training.

Higher experience levels, less leverage, and better training should improve audit quality – and in the long run, drive down the cost of litigation and malpractice insurance. I would also anticipate that reduced turnover and better experience levels would enhance audit efficiency to the point where the efficiencies and cost savings may offset the costs associated with more experienced personnel operating at more reasonable workload levels. I would not anticipate the cost to produce the audit quality metrics to be significant since much of this information is likely already available at most audit firms.

Long story short, transparency should enable market forces to drive to an economic equilibrium point that may be much more economically efficient than where the profession is currently at.

- 18 Would investors have increased confidence in financial reporting as a result of increased audit firm transparency?

Yes – because increased transparency can be expected to improve competition in a manner that improves audit quality.

- 19 Are there significant benefits to investors of increased audit firm transparency, since they invest in companies and not audit firms?

I strongly believe that increasing audit firm transparency will improve audit quality. Improving audit quality benefits investors because the integrity of the capital markets depends heavily on the reliability of the financial information audited by the major firms. Reliable financial information is also essential to maintaining low costs of capital. Anything that can be done cost-effectively to improve audit quality will benefit all concerned, including investors.

End

International Organization of Securities Commissions

Response to Request for Public Comment on Transparency of Firms that Audit Public Companies

Addendum to Robert Conway's November 25, 2009 Public Comment¹

The first question posed by the International Organization of Securities Commissions (IOSCO) in their request for public comment on "Transparency of Firms that Audit Public Companies" asks whether a definition of audit quality is needed to evaluate audit quality or can audit quality be evaluated from an understanding of the attributes, behaviors, and indicators of audit quality? In my November 25, 2009 submission to IOSCO, I listed numerous variables having an impact on audit quality.

I have organized these variables into a one page visual model ("The Audit Quality Pyramid") that appears at the end of this document. It is my hope that the Audit Quality Pyramid can advance the discussion of the interplay between certain audit firm operational metrics and audit quality.

The Audit Quality Pyramid has three fundamental levels: 1) Basic Inputs, 2) Skills and Tools, and 3) Fortitude. Much like a real pyramid, each level builds on the foundation of the lower levels.

The Basic Inputs

The basic inputs are fundamental to a team of people doing any job well – whether it be auditing, surgery, or building a house. To do any of those activities well, the team needs to have the necessary experience, an appropriate amount of time to do the job right, good supervision, and skills which are up to date. In the auditing context, these items are:

- Appropriate Supervision and Review
- Reasonable Partner Workloads
- Reasonable Staff Workloads
- Suitably Experienced Professionals
- Good Audit Team Continuity
- On-Going Continuing Education

As you can see from the bottom of the Audit Quality Pyramid, these fundamentals line up nicely with six "Audit Firm Basic Operational Input Metrics" – the same metrics I cited in my original submission to the Treasury Department's Advisory Committee on the Auditing Profession. If any of these fundamentals are not solidly in place, they jeopardize the team's ability to achieve audit quality. However, these fundamentals do not guarantee that the audit team will get it right. Instead, these fundamentals are prerequisites for "getting it right." There are other elements at higher levels of the pyramid (described below) that must also be in place to ultimately achieve audit quality.

¹ In my original submission to IOSCO dated November 25, 2009, I noted that "The views I express herein are my own and do not necessarily reflect those of the Board, Board Members, or other members of the PCAOB staff." That same disclaimer applies to this document.

Skills and Tools

The next level up on the Audit Quality Pyramid shows the “Skills and Tools” needed to identify auditing and accounting issues and formulate the appropriate corrective action. The “Skills and Tools” are:

- Professional Skepticism
- Technical Competence
- Industry Expertise
- Compliance with a Sound Audit Methodology
- An Environment Conducive to Seeking Consultation
- A Vibrant Risk Management and Technical Resource Function that is Independent of Audit Operations

The “Skills and Tools” listed above do not function in isolation. To function effectively, auditors must have the “Basic Inputs” in place -- which are adequate time, suitable experience, proper supervision and review, and up-to-date skills. Without having the basic inputs in place, the “Skills and Tools” may be rendered ineffective.

The “Basic Inputs” and the “Skills and Tools” will enable the auditor to identify the issues. But the job is not yet complete. There is one more level to the pyramid that is absolutely essential – and also – perhaps the most difficult to quantify: Fortitude.

Fortitude

Issue identification is at the core of the audit process. However, if the auditor does not have the fortitude to stand tall and insist that his or her client correct the identified issues, the audit effort is wasted. There is a tricky set of dynamics that challenge the audit partner’s fortitude to do the right thing. I have listed these dynamics as “External Pressures” that are exerted on the external walls of the Audit Quality Pyramid. Those pressures include:

- Retention of the Client
- Collection of Fees (particularly overages)
- Achieving Engagement Profit Goals
- Tight Deadlines
- Increasing Complexity

To counter these pressures, the Audit Quality Pyramid identifies various elements which bolster the audit partner’s fortitude to “Do the Right Thing.” These elements include:

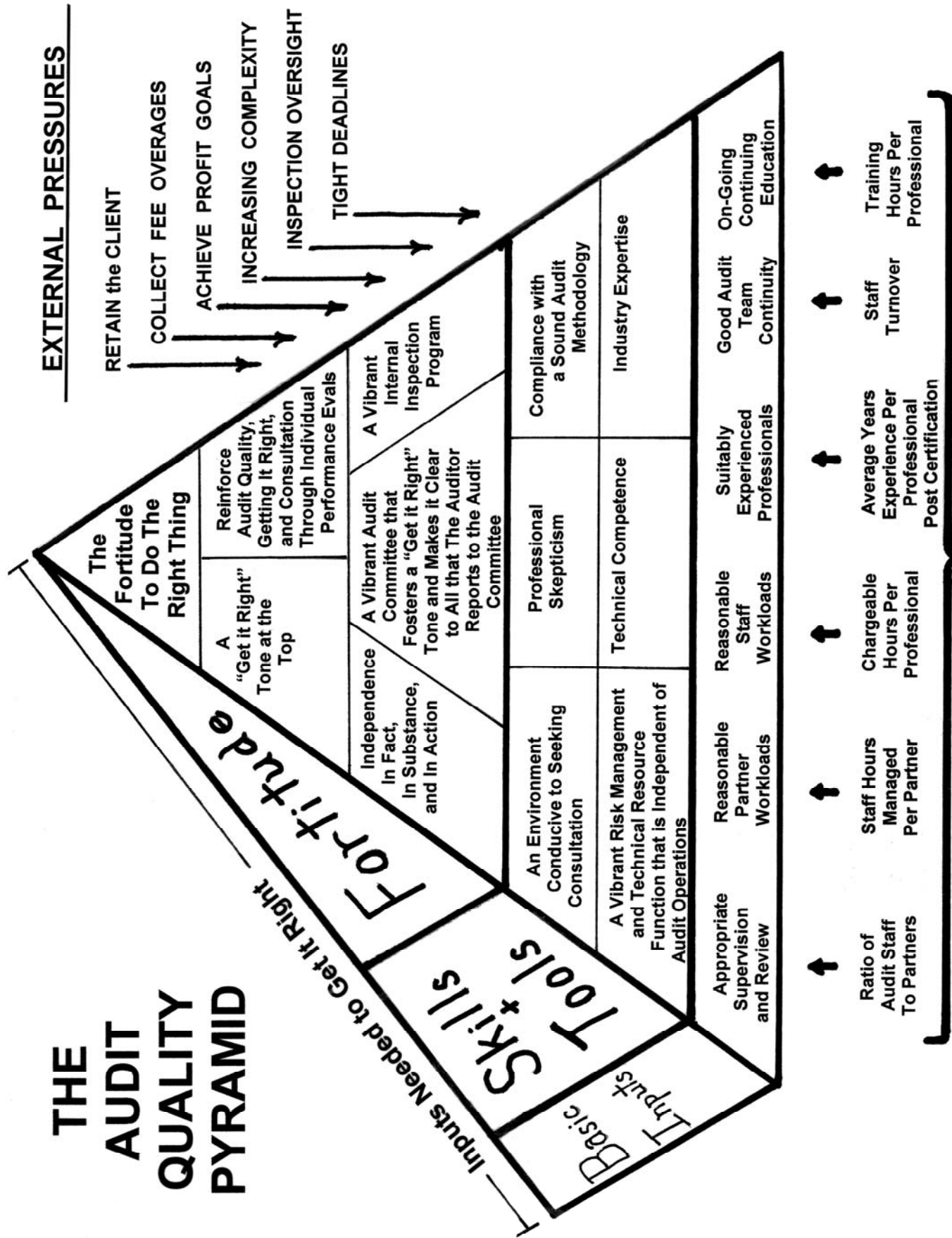
- A “Get It Right” tone at the top of the audit firm.
- Vibrant audit committee that fosters a “Get it Right” tone and makes it clear to all that the auditor reports first and foremost to the audit committee.
- Independence in fact, in substance, and in action.
- A vibrant internal inspection program.
- A performance evaluation and compensation process that reinforces audit quality and “Getting It Right.”

The Importance of the Operational Metrics

The operational metrics I am advocating are not a silver bullet and they are only part of the Audit Quality Pyramid. But they are a very important part of the foundation of the Audit Quality Pyramid. Of particular concern is the notion that the profit motive drives the operational metrics in a direction which is contrary to good audit quality. I continue to believe that the profit motive, left unchecked, has led to an audit firm business model that is characterized by high workloads, high turnover, low experience levels, poor supervision, and professionals who are unable to devote sufficient time to relevant training.

I continue to believe that a low cost / high impact way to improve all of this is to let the free market mechanism do its magic. For that to happen, however, the market place participants need more information than they have currently. In order for the market place participants to make informed decisions that will drive market forces to the proper equilibrium point, the consumers of audit services need to know more about what they are buying and the accounting graduates need to know more about their prospective employers. That is why the transparent disclosure of the operational metrics is so important.

THE AUDIT QUALITY PYRAMID



January 15, 2010

Mr. Greg Tanzer
Secretary General
International Organization of Securities Commissions
Calle Oquendo 12
28006 Madrid, Spain

***Re: Public Comment on the Transparency of Firms that Audit Public Companies:
Consultation Report***

Dear Mr. Tanzer:

Deloitte Touche Tohmatsu appreciates the opportunity to comment on the consultation project initiated by the International Organization of Securities Commissions (“IOSCO”) on the transparency of firms that audit public companies (the “Consultation Report”). The Consultation Report seeks comment on the usefulness of disclosures of audit firm information to investors, audit committees, and other stakeholders, on the one hand, and to audit oversight authorities, on the other, and specifically, on whether those disclosures may serve to improve audit quality and the availability and delivery of audit services.

The Consultation Report notes that disclosures of information related to audit quality are important to investor confidence in financial reporting and the strength and stability of the global capital markets; to decisions of audit committees related to the appointment and retention of the audit firms; and to regulators’ decisions related to professional oversight and investor protection.¹ We agree that the provision of information related to the needs of these various constituencies can be beneficial for enhancing investor confidence. In this regard, we believe that the flow of information between audit firms and

¹ Consultation Report at 1-2.

audit oversight authorities, as well as public disclosures of certain information, such as that relating to firm quality control systems and governance structures, is important, as discussed further below.

As IOSCO recognizes, however, there are significant challenges in identifying information relating to audit quality and in determining whether it is relevant and understandable for investors and other stakeholders.² There currently is no generally accepted definition of audit quality nor consensus on the attributes or indicators of, or behaviors that promote, audit quality.³ Rather, audit quality is fostered through multiple layers of policies, procedures, and controls within audit firms that do not readily lend themselves to measurement or comparability, thereby making assessments as to whether disclosures improve audit quality challenging.

In addition, without the proper context, many potential indicators of audit quality could be misunderstood. For example, assessing the significance of particular information to audit quality typically requires additional background related to the specific details of an audit engagement, and substantial expertise with audit standards and their application. Audit oversight authorities have both expertise and resources that enable them to carefully evaluate and assess information received from audit firms. The robust flow of information between audit firms and audit oversight authorities facilitates the ability of oversight authorities to effectively monitor audit quality. These regulators thus play a key role in protecting investors through the oversight of audit professionals and the audits they perform.⁴ As the Consultation Report recognizes, given the public's ability to rely on such

² *Id.* at 14, 20.

³ *Id.* at 3, 17-18.

⁴ *Id.* at 22.

oversight, information provided to the general public does not need to be as detailed or comprehensive as that provided to such authorities.⁵

To minimize the risk that information disclosed to the general public may be misinterpreted without the proper context and expertise, it is important to ensure that disclosures that are made to investors and other stakeholders focus on conveying information that is understandable. The disclosures required under Article 40 of the Eighth Company Law Directive in the European Union seek to inform investors and other stakeholders about the structure and governance of audit firms, as well as the quality controls that firms have in place to provide audit services. We support the disclosure approach embodied in Article 40 as we believe such disclosures contribute to the understanding of policies and procedures employed to achieve high quality audits. To the extent disclosures are required, we also note that consistency across jurisdictions regarding such disclosures would allow investors and other stakeholders to better understand the information being disclosed.

We address issues related to disclosures to various constituencies below.

I. Disclosures to Audit Oversight Authorities⁶

We believe that independent audit oversight regimes contribute to enhancing audit quality, and we support independent oversight of the profession. Significantly, audit firms currently provide a wide array of information to audit oversight authorities, through registration, inspection and reporting processes. Such disclosures allow these audit oversight authorities the ability, among other things, to oversee the profession generally, to

⁵ *Id.*

⁶ This section includes responses to, or discussion of, certain aspects of questions 4 and 13 of the Consultation Report.

monitor the quality of the audits performed by audit firms, and, where audit work may be viewed as departing from applicable standards, to require appropriate remedial actions.

Audit oversight authorities are best positioned to evaluate information about audit firms and assess its impact on audit quality. Oversight authorities have both expertise and mechanisms in place, including inspections, that enable such authorities to carefully evaluate and assess information received from audit firms, and to engage in further dialogue with audit firms on issues related to quality where appropriate. For example, in situations where the impact on audit quality of certain disclosed information is not clear, audit oversight authorities typically have the expertise and resources to understand what additional information may be needed to evaluate the matter, and the ability to obtain such additional information. Without such context and the ability to access additional information, many disclosures may be misunderstood by investors and other stakeholders. For example, an investor may incorrectly associate restatements with poor quality audits even though, as the Consultation Report notes, a restatement of a company's financial statements does not necessarily indicate the audit performed failed to comply with applicable auditing standards.⁷

In addition, to foster regulatory dialogue and to address legitimate confidentiality concerns, information provided to oversight authorities is often subject to restrictions from public disclosure. The recognition that information will be maintained as confidential not only serves to address client confidentiality concerns and various legal restrictions related to privacy and other matters, but also allows for a more constructive and detailed dialogue between audit firms and audit oversight authorities. This dialogue enhances the ability of such authorities to engage in effective and robust oversight of the profession.

⁷ Consultation Report at 16.

II. Disclosures to Investors, Audit Committees, and Other Stakeholders⁸

As previously discussed, there is no clear definition of audit quality nor consensus on the attributes or indicators of, or behaviors that promote, audit quality. We note, however, that disclosures required under Article 40 of the Eighth Company Law Directive in the European Union provide information that investors, audit committees, and other stakeholders may find useful in understanding and evaluating measures undertaken by audit firms to achieve audit quality. Article 40 sets forth certain requirements for disclosure of audit firm information, including, among other things, information related to an audit firm's governance and legal structure; the structural arrangement of an applicable network; and certain financial information relating to the size of the audit practice, such as the proportion of fees the audit firm derives from audit and from non-audit services. Significantly, Article 40 requires a description of the audit firm's internal quality control systems. Disclosures made in relation to this requirement typically provide detail about, among other things, policies and practices for consultations, reviews, and client acceptance and continuance. This discussion about an audit firm's quality control systems should provide beneficial information for parties that review Article 40 reports.

We support the approach in Article 40 for disclosures to investors, audit committees, and other stakeholders. Many audit firms have already published reports required by Article 40,⁹ and increasing numbers of audit firms will do so as additional European Member States implement Article 40 and as other audit firms become subject to compliance with the requirement. At the same time, investors, audit committees, and other stakeholders are gaining familiarity with Article 40 disclosures. Further experience with

⁸ This section includes responses to, or discussion of, certain aspects of questions 4 and 12 of the Consultation Report.

⁹ Consultation Report at 9.

these disclosures over the coming years will help identify the extent to which these disclosures contribute to investors' understanding of measures taken to achieve audit quality. In addition, consistency across jurisdictions regarding public disclosures, such as those required by Article 40, would allow investors to better understand and evaluate the information being disclosed. Accordingly, where public disclosure of audit firm information is contemplated, we urge that regulators model such disclosure requirements on the Article 40 approach.

III. Considerations Related to Alternative Disclosures¹⁰

As noted above, a key consideration in evaluating the usefulness of disclosures to the general public is the extent to which such disclosures are relevant to audit quality and understandable by investors and other stakeholders. We believe that the relevance of a particular disclosure to these parties should be balanced against the risk that the disclosure may be misinterpreted. By way of example, we note that the Consultation Report suggests that the disclosure of "input" measures to investors and other stakeholders may be appropriate.¹¹ Input measures identified in the Consultation Report include, for example, employee hours worked per week, average number of clients per partner, utilization percentages, and leverage ratios. We have concerns, however, about the usefulness of such information to investors and other stakeholders and the risks that might flow from these disclosures. Moreover, such disclosures may even be misleading to them, in part, because it will not be apparent how these measures might impact audit quality. These input measures inevitably would lack sufficient context to allow investors and other stakeholders the ability to undertake meaningful analysis of the information. In particular, we do not

¹⁰ This section includes responses to, or discussion of, certain aspects of questions 7, 8, 9, 14, 17 and 20 of the Consultation Report.

¹¹ Consultation Report at 14-15.

believe the input measures in isolation lend themselves to comparability across engagements.

For example, one engagement team might spend more time than another engagement team on a comparably sized company because the first engagement team has identified a greater number of adjustments, or significant accounting events have taken place during the engagement period (such as implementation of new accounting policies or a new control system). The additional time spent, while necessary under the facts and circumstances, would not necessarily make that audit of higher quality than an audit that took fewer hours in a less complex situation. Without adequate context, however, an input measure, such as employee hours worked, would provide little insight into the audit quality of the respective engagements. Similarly, some engagements may require higher partner-to-staff leverage ratios based on the size, scope, risk and complexity of the engagement. The number of engagements a partner manages also will vary depending on the size and complexity of each client. It is unclear how these input measures could adequately convey meaningful information about audit quality without factoring in additional considerations, which might include the complexity and risk of an engagement.

As a result, we believe there is a risk that input measures, if disclosed to investors and other stakeholders, could lead to the creation of benchmarks or targets that are misapplied and misunderstood by investors and other stakeholders. These benchmarks or targets also could adversely affect audit quality if engagement management is focused on achieving such metrics, rather than appropriately addressing risks and complexities that may be present in a particular engagement.¹² In contrast, audit oversight authorities have the expertise, and, where appropriate, the mechanisms in place to gather additional facts

¹² *Id.* at 18.

necessary to put this information in the proper context, and thus, to the extent there is relevant information, are more likely to understand how it might impact audit quality.¹³

We also believe that the potential disclosures to investors, audit committees and other stakeholders should be balanced against the risks and burdens to audit firms that may result from making such disclosures. Such risks and burdens include, for example, those arising in the context of performing audits for multi-national corporations. Audit firms that provide such services could become subject to requirements for disclosure of audit firm information imposed by multiple jurisdictions outside their home country. In addition to the burdens that arise from having multiple disclosure regimes, legal conflicts and other restrictions may arise under certain home country laws that preclude or affect an audit firm's ability to provide information. These conflicts may limit the extent to which certain information, such as that related to employee workload and legal proceedings against the audit firm or individuals, can be disclosed. Such conflicts could place audit firms in the untenable position of having to decide whether to comply with foreign disclosure requirements and risk violating home country law, or to comply with home country law and risk violating the foreign disclosure requirements. Mutual reliance on home country disclosures, under which audit firms effectively are subject to disclosure requirements only under home country laws, could serve to alleviate some of these problems.

To the extent disclosures are made, however, we again emphasize that consistency of public disclosures across jurisdictions would allow investors to better evaluate the disclosed information and facilitate audit firms' efforts in making disclosures. By contrast,

¹³ Other potential disclosures identified in the Consultation Report also could prove misleading, such as those suggested for describing certain aspects of the relationship between audit firms and their networks, which appear to misapprehend the role and operation of audit firms and their networks. *See, e.g.*, Consultation Report at 10 (proposing potential disclosures related to “[h]ow global networks ensure compliance with standards in all jurisdictions in which the audit firm operates” and disclosures related to “[t]he balance of power between the entire network compared to the country-wide firm level”).

inconsistencies in disclosure regimes may inhibit comprehension of the information disclosed and may also drive up the costs of compliance. Such increased compliance costs may, among other things, hinder the entry of small and mid-sized audit firms in the market for providers of large public company audit work and thus may negatively impact the availability of audit services.

Finally, public disclosures related to an audit firm's financial information discussed in the Consultation Report should be carefully considered for several reasons. First, there is ongoing debate as to the usefulness of such disclosures to either promoting or understanding audit quality, and we are not aware of evidence to suggest that audit firm financial information is useful in assessing audit quality. Second, there is a risk that such disclosures could be misused and could increase risks related to litigation in certain jurisdictions. Although some jurisdictions currently require public disclosures of certain financial information,¹⁴ such disclosures may not be suitable in all jurisdictions. In the United States, for example, where the litigation environment is particularly challenging, disclosure of audit firm financial statements could have the unintended result of encouraging plaintiffs to file suits that lack merit against audit firms or to seek unwarranted settlements based on this information. As the Consultation Report notes, these litigation related consequences could harm competition among smaller and mid-sized audit firms, and could ultimately have an impact on the sustainability of the profession.¹⁵ It should be noted that, although audit oversight authorities have access to certain financial information, because such information is generally maintained as confidential by oversight authorities,

¹⁴ As the Consultation Report notes, certain countries such as the Netherlands and the United Kingdom currently require financial statements of audit firms to be publicly disclosed in specified circumstances. Consultation Report at 20 & n.40.

¹⁵ *Id.*

providing this information to oversight authorities generally does not present the same litigation or concentration-related risks as discussed above.

* * *

Regulators play a key role in protecting investors through diligent oversight of audit professionals and the audits they perform, and, given investors' ability to rely on such oversight, information provided to the general public should not be as comprehensive as that provided to such authorities. To the extent public disclosures by audit firms are required, Article 40 provides disclosures that are understandable and that may be useful in evaluating measures undertaken by audit firms to achieve audit quality. If further study is undertaken to assess the utility of potential public disclosures beyond those contained in Article 40, however, we believe that such study should consider the relevance of a particular disclosure not only to audit quality, but also the relevance of such disclosures to investors and other stakeholders. Providing a number of disclosures with no nexus to audit quality will not serve to benefit investors or the capital markets. Moreover, any disclosures should be balanced against the risk that the disclosure may be misunderstood or misinterpreted, and the risks and burdens to audit firms relating to such disclosures. We would encourage the involvement of all relevant stakeholders, including investors, the International Forum of Independent Audit Regulators and individual audit oversight authorities, audit firms, and IOSCO, and we would welcome the opportunity to participate in any such study.

We thank IOSCO for circulating the Consultation Report and appreciate the opportunity to comment on it. If you have any questions concerning our comments, please contact Charles A. Horstmann at +1-212-492-3958 or J. Denise Pacofsky at +1-212-492-2841.

Yours very truly,

Deloitte Touche Tohmatsu

Level 13, The Gate
P.O. Box 75850, Dubai, UAE.
Tel: +971 (0)4 362 1500
Fax: +971 (0)4 362 0801
Email: info@dfsa.ae

By E-mail

Greg Tanzer
Secretary General
IOSCO General Secretariat
Calle Oquendo 12
28006 Madrid
Spain

AuditorTransparency@iosco.org

Dear Sir / Madam,

**Comments on the Transparency of Firms that Audit Public Companies
Consultation Paper**

The Dubai Financial Services Authority has taken this opportunity to provide commentary on the Transparency of Firms that Audit Public Companies Consultation Paper. We consider this to be a comprehensive paper hence our comments which are set out in an attachment to this letter are rather limited.

We are happy to provide any further elaboration or clarifications on the issues raised and can be contacted on +971 4362 1549 or by e-mail on nlalani@dfsa.ae.

We look forward to participating in any further work in this area.

Yours sincerely



Christian Cameron
Manager
Policy and Legal Services

**Comments on Consultation Report
Transparency of Firms that Audit Public Companies**

November 26, 2009



The DFSA is the independent financial services regulator for the DIFC

www.dfsa.ae

Question 1

Is a definition of audit quality necessary to evaluate audit quality or can audit quality be evaluated from an understanding of the attributes, behaviors, and indicators of audit quality?

Any definition of Audit quality would be subjective and would be incomplete without attributes, behaviors, and indicators.

Audit quality can be best evaluated from an understanding of the attributes, behaviors, and indicators of audit quality therefore a comprehensive definition of audit quality is not necessarily required.

Question 2

In addition to competence and industry expertise of the audit personnel, firm culture that promotes audit quality, firm-wide quality control systems, and auditor oversight, are there other examples of attributes, behaviors, and indicators of audit quality that should be considered?

As a starting point, the above mentioned examples are sufficient.

Question 3

Are there other areas of governance for which additional transparency should be considered?

The four broader areas cover the transparency objectives for governance. These areas are not exhaustive and will evolve over time.

Question 4

Would the proposed disclosures mentioned above be useful in improving audit quality and availability and delivery of audit services to public companies?

The proposed disclosures mentioned above may be useful in improving audit quality and availability and delivery of audit services to public companies.

Question 5

Could other limitations arise if such disclosures were required?



Limitation may include consumption of a significant amount of time in preparing these disclosures, thus reducing the time available to perform the actual audits. This may also result in increased costs which may ultimately be passed on to the clients to maintain the required profitability.

Question 6

Can audit quality indicators provide objective information when evaluating a firms' audit quality? If so, do the ones identified in this report accomplish that goal?

Audit quality cannot provide objective information when evaluating a firms' audit quality as these are subject to subjective nature of the concept of audit quality.

However, the indicators identified in this report would be the first step in accomplishing the goal.

Question 7

In addition to the indicators identified in this report, are there any other audit quality indicators that should be considered for disclosure? Would disclosure of the audit quality indicators described above be helpful in evaluating audit quality?

As mentioned above, these indicators would be the first step in accomplishing the goal. Although these indicators would be helpful in evaluating audit quality, the evaluation would remain subjective due to inherit subjective nature of the indicators.

Question 8

In addition to the benefits or limitations identified in this report, are there any other benefits or limitations about disclosing audit quality indicators that need to be considered?

There may be other benefits or limitations about disclosing audit quality indicators which will evolve during time. Without evaluating the impact of these quality indicators, it is difficult to identify other benefits or limitations.

Question 9

Can audited financial statements of audit firms provide useful or objective information regarding audit quality? If so, how?

The audited financial statements of audit firms may not provide useful information regarding audit quality but it would certainly provide greater transparency, increase discipline, and help build accountability and trust.

Question 10

If disclosure to the public or regulators of an audit firm's own audited financial statements is warranted, who should audit the auditors? Are firms other than the Big Four equipped to audit the Big Four? If not, does having the Big Four firms audit each other raise concerns? If so, how could any such concerns be addressed?

If disclosure to the public or regulators of an audit firm's own audited financial statements is warranted, a body independent of these audit firms should audit the auditors. This also eliminates the concerns from having Big Four firms audit each other.

Question 11

Can disclosing certain financial information instead of audited financial statements achieve the same objective of improving audit quality and the availability and delivery of audit services? If so, what financial information should be disclosed?

Disclosure of certain financial information instead of audited financial statement may achieve the same objective of improving the audit quality and the availability and delivery of audit services. The information can include firm's investment in the proprietary audit software, training and development, compensation and benefits, professional indemnity insurance, claims against professional indemnity insurance etc.

Question 12

Are there other parameters that should be considered?

None at this time. Other parameters may evolve over time.

Question 13

Should certain disclosures not be publicly available and if so, what criteria should be considered when determining what disclosures should be publicly available?

Making all disclosures public would largely depend on the sensitivity involved. There cannot be one criterion to determine the same.



Question 14

Should certain disclosures be made at the network, firm, and/or, engagement level?

As a starting point, firm wide disclosure would do the needful.

Question 15

Should there be different disclosure requirements for large, mid-size, and small audit firms?

The disclosure requirements should be same for large, mid-size and small audit firms. It is only that small firms may lack details to the extent large and mid-size audit firms are able to provide.

Question 16

Should the disclosures be mandatory and if so, should they be subject to regulatory oversight? Would a similar impact to the markets occur if the disclosures were encouraged instead of being mandatory? Should consideration be given to a framework of audit quality and allow for flexibility in the types of disclosures?

Ideally, the disclosures should be mandatory and should be subject to regulatory oversight. If disclosures are encouraged and are not mandatory, the impact to the markets would not be the same. Some firms may opt to disclose to the extent which is beneficial to them.

Considerations may be given to a framework of audit quality and allow for flexibility in the types of disclosures.

Question 17

Would transparency of audit firms improve audit quality and the availability and delivery of audit services? What negative effects, including costs, of increased transparency should regulators consider?

Transparency of audit firms may improve audit quality and the availability and delivery of audit services.

The negative impacts would be increased costs which may ultimately be passed on to the clients to maintain the required profitability.

Question 18

Would investors have increased confidence in financial reporting as a result of increased audit firm transparency?

Increased audit firm transparency would certainly increase investor's confidence in financial reporting. However, this should be noted that transparency is not the single driver for this confidence.

Question 19

Are there significant benefits to investors of increased audit firm transparency, since they invest in companies and not audit firms?

It is true that investors do not invest in the audit firms but they invest in companies based on the financial strength as audited by these audit firms. Increased transparency would give investors the required confidence in the audit firm which would result in evaluating the investments prospects on which they invest in companies thus making an informed decision.

Question 20

Should regulators consider areas outside of audit firms' governance, audit quality indicators, and financial statements for potential disclosures?

As a starting point, regulators should only consider areas of audit firms' governance, audit quality indicators and financial statements for potential disclosures.

Greg Tanzer
Secretary General
International Organization of Securities Commissions
C / Oquendo 12
28006 Madrid
Spain

15th January 2010

Dear Mr Tanzer

Transparency of Firms that Audit Public Companies

We welcome the IOSCO paper on transparency of firms that audit public companies. EGIAN's membership is made up of 21 global organisations which offer audit, accounting and business advisory services. The combined turnover of our members is US\$ 34 billion. In this response we set out our views and would be very pleased to discuss them in more detail with you if that would be helpful.

The members of EGIAN that audit public companies, and other public interest entities, believe that transparency by audit firms can contribute to an improvement in audit quality. Some member firms of EGIAN are already subject to national obligations to publish audited financial statements, and many firms will be presenting "transparency reports" as required by national legislation implementing Article 40 of the EC 8th Directive.

We have preparing our responses by way of addressing each of the questions posed in the paper.

Yours sincerely,

Andrew Brown, Chairman

POSSIBLE EFFECTS OF TRANSPARENCY RELATED TO AUDIT QUALITY AND AVAILABILITY AND DELIVERY OF AUDIT SERVICES

1. Is a definition of audit quality necessary to evaluate audit quality or can audit quality be evaluated from an understanding of the attributes, behaviours, and indicators of audit quality?

We agree that the concept of “audit quality” is difficult to define. We also agree that different stakeholders will have different perceptions as to the meaning of “audit quality”. It is important that a definition of “audit quality” is agreed upon. This will ensure that auditors, preparers and users of financial information, and other stakeholders can all work from a common base. Having established a common definition, then the attributes, behaviours and indicators of “audit quality” can be determined.

As a working concept we consider that the definition used by the UK Financial Reporting Council in *The Audit Quality Framework* provides a basis of a definition that could be developed more widely in an international context. We also note that the *Audit Quality Forum* of the Institute of Chartered Accountants in England & Wales has for some years brought together interested parties in financial information and auditing, and has issued several papers on the application of the concept of audit quality. IOSCO may find it useful to consult these papers which can be found at www.icaew.com.

2. In addition to competence and industry expertise of the audit personnel, firm culture that promotes audit quality, firm-wide quality control systems, and auditor oversight, are there other examples of attributes, behaviours, and indicators of audit quality that should be considered?

The examples given are an appropriate set of attributes, behaviours and indicators of audit quality.

In a wider sense, a full perspective of the components of audit quality can be determined by reference to International Standard on Quality Control (ISQC) 1 *Quality control for firms that perform audits and reviews of historical financial information, and other assurance and related services engagements*. ISQC 1, issued by the International Audit & Assurance Standards Board (IAASB), lists the following elements of a quality control system for an audit firm:

- Leadership responsibilities for quality within the firm. Ethical requirements;

- Acceptance and continuance of client relationships and specific engagements;
- Human resources;
- Engagement performance; and
- Monitoring.

All of these elements may themselves be regarded as attributes, behaviours and indicators of audit quality in their own right.

TRANSPARENCY OF AUDIT FIRMS' GOVERNANCE

3. Are there other areas of governance for which additional transparency should be considered?

We do not believe that there are any other areas of governance for which additional transparency should be considered.

4. Would the proposed disclosures mentioned above be useful in improving audit quality and availability and delivery of audit services to public companies?

The proposed disclosures would improve third party understanding of the operations of audit firms and this will enhance the understanding of audit quality. Disclosures alone will not broaden the market of providers of audit services to public companies. However, greater awareness by third parties as to how networks and firms ensure that they achieve recognised measures of audit quality will enhance confidence and together with other measures might assist in broadening the range of providers.

5. Could other limitations arise if such disclosures were required?

The paper correctly notes the risk that governance disclosures become “standardised”. As with any governance disclosures it is important that regulators and standard setters ensure that this does not happen. For example, the UK Financial Reporting Council strongly counsels UK public companies against presenting “boilerplate” governance disclosures.

TRANSPARENCY OF AUDIT FIRMS' AUDIT QUALITY INDICATORS

6. Can audit quality indicators provide objective information when evaluating a firm's audit quality? If so, do the ones identified in this report accomplish that goal?

As audit quality is difficult to define then it is appropriate to present a series of measures that can provide objective information when evaluating a firm's audit quality.

The measures identified could accomplish this goal. However, users of reports prepared by firms will have to interpret the information disclosed. There is also the risk that presenting too many measures may result in "information overload" and mean that the goal is not accomplished. The paper presents a long list of both input and output measures. Were all the measures mentioned to be required, then the resulting reports would be costly to prepare and potentially overloaded with information.

As a starting point, the most important measures of quality need to be determined. In our view, this is the results of inspections from external regulators. As regulatory processes are becoming increasingly transparent, then in turn, public reporting of the regulatory process provides an objective measure of audit quality.

7. In addition to the indicators identified in this report, are there any other audit quality indicators that should be considered for disclosure? Would disclosure of the audit quality indicators described above be helpful in evaluating audit quality?

As we comment above, the list of measures presented are extensive, and if all were presented would result in excessive disclosure. Therefore we believe that there are no further indicators that should be added to this list.

In addition, as we comment above, the results of external regulatory inspections are the most relevant measures of audit quality for disclosure.

8. In addition to the benefits or limitations identified in this report, are there any other benefits or limitations about disclosing audit quality indicators that need to be considered?

Indicators of audit quality will be most beneficial if they are objectively presented, and "information overload" is avoided. It is important to assess cost / benefit and ensure that the effort needed to present the indicators required in a public report does not become so costly to prepare that the benefit from the transparency is undermined. In addition, the demands of public reporting must not become so great that smaller, but perfectly competent firms, are not discouraged from engaging in public company auditing.

TRANSPARENCY OF AUDIT FIRMS' FINANCIAL STATEMENTS

9. Can audited financial statements of audit firms provide useful or objective information regarding audit quality? If so, how?

Audited financial statements of firms provide third parties with objective information as to the financial stability and standing of the firm. Financial stability and soundness should be seen as a measure of audit quality. A firm which is not financially strong may be perceived as being at risk, and lacking the resources and potentially the state of mind to deliver audit quality.

10. If disclosure to the public or regulators of an audit firm's own audited financial statements is warranted, who should audit the auditors? Are firms other than the Big Four equipped to audit the Big Four? If not, does having the Big Four firms audit each other raise concerns? If so, how could any such concerns be addressed?

Registered audit firms should audit the financial statements of other audit firms. In the United Kingdom this has been the case, without issue, for some years. In addition, in the United Kingdom it is the fact that the Big Four audit firms are audited by non-Big Four firms. The capabilities of the not Big Four auditors have not been an issue and there is no evidence of “audit failure” in terms of the audited financial statements published by Big Four firms. There is no reason as why the United Kingdom experience of external audit of audit firms cannot be replicated in other countries.

11. Can disclosing certain financial information instead of audited financial statements achieve the same objective of improving audit quality and the availability and delivery of audit services? If so, what financial information should be disclosed?

We believe that the publication of audited financial statements by audit firms, subject to appropriate size criteria to exempt smaller firms, is the most means of disclosing financial information about firms.

PARAMETERS OF ENHANCED DISCLOSURE FOR AUDIT FIRMS

12. Are there other parameters that should be considered?

There are no other parameters to consider.

13. Should certain disclosures not be publicly available and if so, what criteria should be considered when determining what disclosures should be publicly available?

Financial statements should be prepared in accordance with recognised financial reporting frameworks, and should not be extended to require the public disclosure of the individual compensation of principals in the firm.

Cost / benefit is important, and disclosures should be reduced (or made voluntary) for firms that fall below either specified financial size criteria or which have a small number of public interest clients.

Transparency disclosures should be made at either the network or country level. A way of applying this would be for disclosures to be made at the “legal entity” level, recognising that some firms are now “cross border”. To achieve transparency, disclosures must be given for the firm as a whole, and not limited to the audit practice. Principles of substance therefore need to be applied to ensure that disclosures are given for the “complete entity”.

It is probably inappropriate to require detailed disclosure at the individual engagement level, and the exchange of information over and above that which is in the public arena about the firm as a whole, should be left to the firm and the audit committee.

14. Should certain disclosures be made at the network, firm, and/or, engagement level?

This is addressed under 13 above.

15. Should there be different disclosure requirements for large, mid-size, and small audit firms?

As we note under 13 above, there should be reduced disclosures for smaller firms. A “smaller” firm should be defined by reference to either financial size criteria or the number of “public interest” audits.

16. Should the disclosures be mandatory and if so, should they be subject to regulatory oversight? Would a similar impact to the markets occur if the disclosures were encouraged instead of being mandatory? Should consideration be given to a framework of audit quality and allow for flexibility in the types of disclosures?

Disclosures should be mandatory. Regulatory oversight will ensure consistency of presentation and delivery of disclosures. Regulatory oversight is best provided by audit regulators as part of their ongoing regulatory activities.

There should be a framework for audit quality. There should be a principles based framework, requiring disclosures on a “comply or explain” basis. The framework should encourage an individual style of disclosure and discourage a “boilerplate” approach.

17. Would transparency of audit firms improve audit quality and the availability and delivery of audit services? What negative effects, including costs, of increased transparency should regulators consider?

Greater transparency will improve audit quality as firms will need to deliver audits consistent with their public statements. Transparency will not alone broaden the number of providers of audit services, but taken with other measures, it could assist with increasing the availability and delivery of audit services.

The delivery of this information does have a cost, and cost / benefit needs to be assessed in developing a framework for quality and a set of disclosures. Regulators must also avoid “information overload” in requiring the publication of excessive disclosures which will ultimately provide limited benefit to users.

18. Would investors have increased confidence in financial reporting as a result of increased audit firm transparency?

We have not encountered any comment from clients or investors that greater audit firm transparency will increase confidence in financial reporting.

19. Are there significant benefits to investors of increased audit firm transparency, since they invest in companies and not audit firms?

The benefit to investors is indirect as they invest in companies and not audit firms. Greater transparency of audit firms will not itself increase confidence in financial reporting.

20. Should regulators consider areas outside of audit firms’ governance, audit quality indicators, and financial statements for potential disclosures?

At this stage, governance, audit quality indicators and financial statements are a sufficient source of disclosures.



IOSCO General Secretariat
Secretary General
Greg Tanzer
Calle Oquendo 12
28006 Madrid
Spain

Subject: Public Comment on the Transparency of Firms that Audit Public Companies, on the Auditor Communications and on the Exploration of Non-Professional Ownership Structures for Audit Firms: Consultation Reports
Ref.: 2.009.068
Amsterdam, 10 December 2009

Dear Mr. Tanzer,

Eumedion, the Dutch corporate governance forum for institutional investors, is pleased for having the opportunity to comment on three related consultations of the Technical Committee of IOSCO on 'Transparency of Firms that Audit Public Companies', 'Auditor Communications' and 'Exploration of Non-Professional Ownership Structures for Audit Firms'. The three consultations contain analyses and questionnaires in order to obtain input from investors, audit oversight authorities, industry and other relevant stakeholders.

By way of background, Eumedion is the Dutch corporate governance forum for institutional investors. Eumedion has 65 Dutch and foreign institutional investors as participants at present. Together they have more than 1 trillion Euro of assets under management. Eumedion's participants invest for Dutch beneficiaries and in listed companies worldwide.

Eumedion supports and appreciates the work that the Technical Committee of IOSCO has undertaken. Many of the issues raised in the report are related to the interests of institutional investors. Since the financial reporting crisis of 2001/2002, society, securities regulators and institutional investors alike paid more attention to the role of auditors in the capital markets. It is fundamental that institutional investors have sufficient, relevant and transparent information upon which they can base their investment decisions. Audits are designed to enhance the degree of confidence of investors and users in financial reports. Therefore, investors have a tremendous interest in auditors' and audit firms' competence, independence, transparency and communications - which all contribute to audit quality.

Some issues mentioned in the report on Transparency of Firms that Audit Public Companies and the report on Exploration of Non-Professional Ownership Structures for Audit Firms fall outside the scope of Eumedion's objectives. Therefore, we have focused our comments on specific elements in these two reports. At the end of our contribution, we answer the four specific questions raised in the consultation on Auditor Communications.

Consultation report on transparency of firms that audit public companies

Transparency of audit firms may have, directly or indirectly, a positive effect on institutional investor's confidence in financial reporting of listed companies and the way the reporting is audited. Transparency applied by audit firms contributes to an environment in which audit firms compete not solely on factors as reputation, size and audit fees. This is important, as competence and experience of auditors and firm's governance (e.g. quality control systems, safeguards against conflicts of interests, and education programs) are other relevant factors for audit quality.

We believe disclosure requirements could sharpen the focus of audit firms on important aspects of audit quality control. Enhanced disclosure may influence how audit firms internally manage audit quality. Only with disclosure we can compare quality control measures between audit firms. By including other information that institutional investors and other users may have, a better judgment of audit quality is facilitated. We therefore generally support IOSCO's approach to consider further transparency of audit firms.

In our view, transparency is needed on potential conflicts of interest as well. We must have an insight into internal governance measures to prevent conflicts of interest. We must know which audit firms offer which audit-related services and which non audit-related services (e.g. tax and consulting services) to the same companies, as well as the aggregated fees applicable.

Considering enhanced transparency, it should be taken into account as well that in the European Union a substantial framework of disclosure requirements for audit firms, including elements of firm governance, already exists. In fact, the requirements, based on EU Directive 2006/46/EC¹, are relatively new. EU Members States were required to implement the disclosure measures by June 2008. We believe that further initiatives on disclosure should be approached carefully - as the effectiveness of the existing disclosure framework has not been evaluated yet.

¹ Directive 2006/46/EC of the European Parliament and of the Council of 17 May 2006 on statutory audits of annual accounts and consolidated accounts, amending Council Directives 78/660/EEC and 83/349/EEC and repealing Council Directive 84/253/EEC (OJ L 157).

Consequently, if it is decided to provide enhanced transparency of audit firms, we will suggest to encourage further disclosure by non binding recommendations first. If these prove to work in practice, one could consider including elements in legal requirements. At the same time, if it would turn out that just a few audit firms comply with these possible recommendations, it could be discussed whether it would be appropriate to turn the recommendations in legislation afterwards.

Exploration of Non-Professional Ownership Structures for Audit Firms

As legislation requires public companies to disclose audited financial reporting and that investors must rely on these audits, the continued availability of independent and high quality audit services is fundamental. We believe that the high degree of concentration in the audit services market for large public companies is an issue of serious concerns. More competition is needed. However, the current ownership and governance rules within audit firms stimulate conservatism. In our view, it is just a question of time before the private partnership model will no longer be tolerated by the users of audit services, as many audit partners – also those without extraordinary performance – become extraordinarily rich, while the governance of some of these firms is relatively poor. It is just a matter of time before people recognize that by introducing a 21st century business model for audit firms one could carve out the dead wood in the partnership structure. This will contribute to the functioning of audit firms, will make their pricing more reasonable and by allowing career opportunities which are less focused on 'all or nothing' create a more healthy and open internal control structure. Besides that, the existing firms tend to focus on existing markets and development of value-adding services for existing markets and clients. While we as investors would like to seek the opportunities in new developing markets and regions, for example in China.

Due to legal ownership restrictions almost all firms are organized as private partnerships and do not raise capital through public markets. The existing restrictions on ownership of audit firms can avoid firms from accessing non-private capital that could be used to develop firms in order to be able to audit large public companies and challenge the Big Four. Currently, by lack of a true alternative, clients of audit firms show signs of conservatism. Many large public companies have business activities in international markets and the complexity of their industries impacts their financial reporting. Those companies simply require audit firms with international coverage. As a result, no new firms have managed to compete structurally with the Big Four in the market since Arthur Andersen collapsed.

Opening up the audit market for large public companies could have several advantages. The most important ones are swift access of investors to new emerging markets and the entrance of new audit market players. Reducing ownership barriers may contribute to the availability of choice of audit services for large public companies. Allowing for non-practitioner ownership may create more alternatives and safeguards for large public companies and their investors, in case one of the Big Four unexpectedly gets involved in an Arthur Andersen scenario.

We recognize the potential risks associated with changes in ownership rules on auditors' independence, professionalism and long term public interest focus. However, we believe that these risks can be reduced by implementation of practical solutions. Under the current ownership rules, risks to auditor independence and quality exist as well. One should not forget that the most important stakeholder of audit firms are the users of financial information, *i.e.* the investors. Investors are dependent on the quality of audit and are those that pick up the bill for the audit services provided. A profit maximizing strategy *vis-à-vis* holdings in audit firms will jeopardize the sustainable profitability of all other investments. Hence, there is an automatic incentive to go for quality; perhaps an even better one than current 'guarantees'. Consequently, we do not believe that external shareholders have an incentive to take decisions in an audit firm that would hamper audit quality.

However, a minimum of proportional safeguards to protect audit quality, others than those related to practitioner ownership, must be put in place. Strengthening audit firms' quality control networks and independence standards, as well as introducing new structures in firms' governance, for example board of directors with a more independent mindset, might create such safeguards. Currently audit partners are supervised by audit partners of the same firm. This is suboptimal supervision.

The introduction of non-practitioners in the governance of firms is needed. We would, however, not be in favor of the concept of "passive non-practitioner ownership" (non-binding voting) as a way of avoiding potential conflicts of interests within audit firms. That would intervene with the principle of "one share one vote" which is generally recognized as an important element of appropriate corporate governance. We doubt whether the range of potential non-practitioner owners should be limited. The composition of the board must be a fair constellation of the true constituents, the users of audit services. The personalities that serve in those boards must be carefully selected. In fact, introducing substantial restrictions *ex-ante* could have a negative influence on the ability of audit firms to raise capital, which should be, as a matter of fact, an open choice. Audit firms' existing option for debt funding can in our view not be seen as a strong argument not to enhance the access to equity financing. It could be valuable for audit firms to

have a choice between debt finance and equity finance in order to raise substantial funds, both in going concern and when times get tough.

Auditors communication

As far as the Consultation Report on Auditors Communications we would like to respond as follows:

Question 1. Is the standard audit report useful to investors? If not, why?

The existing standard is to some extent useful for institutional investors, since it offers investors an impression of the auditors' view on the financial statements and the basis for that view. Nevertheless, we believe the audit report could be much more valuable for investors. For the purpose of investors' decision making, it can be worthwhile when further information on the audit process (what the auditor actually did) and the quality of the financial statements (level of conservatism in management accounting decisions, analyses of risks) would be included in the audit report. Hence, we are in favor of requiring auditors to disclose the report of assumptions as well as a summary of the management letter without elaborate disclaimers. Investors and other users should be offered more information on the auditor's work on risk management, risk monitoring as well as relevant sensitivity analyses. At the same time, disclosure must be to the point and focus on only a few substantial issues. Extensive overviews and graphs can be left to the domain of auditors *vis-à-vis* audit committees.

Question 2. Would investors prefer a more concise audit report (e.g. a one-sentence report that includes only the auditor's opinion on whether the financial statements are fairly presented)? If so, why? etc.

The current form and language of the audit report are highly standardized. Due to its "pass/fail model", any "in between" is not allowed. As a consequence, the auditor can not truly weigh the quality of financial reporting and express this in their opinion. The level of standardization causes persons to become so familiar with the wording that the informational value is close to zero, while the audit report should be the most important form of communication between auditors and investors. A more tailored report that for instance reflects the judgments by the auditor throughout the audit process may enable investors to better understand the financial statements and the performed audit. The possibility to include findings on specific reviews called for by the investors and which had been reflected in engagements letters would facilitate a steep increase in the informational value of audit opinions and better reflect the actual principle-agent connection between investors and auditors.

Question 3. Are investors receiving information about the audit that they need to make informed investment decisions? If not, who should provide this information, the management or the auditor?

It is difficult to answer this question in general, since the adequacy of received information varies from case to case. However, we believe that further disclosure of relevant information by the auditor and/or the company will primarily decrease the risk investors do not have enough information to take appropriate investment decisions. It is important that the disclosed information not only focuses on financial facts and figures, but also includes relevant non financial and quality issues. In concrete terms, we would support when more information is provided on the scope and conduct of the audit, the consistency of company's accounting policies and the quality of financial statements in terms of clarity and verifiability. In our view, by providing a more concise audit report, investors will be able to better understand the audited financial information and its context. We prefer having as much as possible additional audit information included in the audit report. Providing additional information outside the report, for example in appendixes or additional documents, might negatively affect the coherence of the auditor's communication.

Question 4. If new or revised auditor communications are desired, would such communications be practicable? What legal, regulatory and practical challenges would preclude such communications? What criteria or principles should regulators use to determine what additional information should be provided?

We recognize revising audit communications, depending its form and extent, could result in certain legal, regulatory en practical challenges. Given, however, the public interest of audit functioning as a safeguard for the reliability of financial reporting in order to protect investors and other users, we are convinced that the benefits will outweigh these potential problems. Some of the potential problems, for example the need to amend existing legislation and audit standards, do not have a structural nature. Of course, the costs of more communications should not become excessive. At the same time, as investors ultimately pay these costs, it should be them to worry about "the bill" most. By and large, we believe that the challenges faced could be overcome.

When considering to what extent additional auditor communications are needed users' interests should be the primary objective, as referred to page 1 of the consultation paper. Investors and other users heavily depend on receiving adequate and reliable information from both listed companies and auditors, for them to take appropriate investment decisions. When this is



If you would like to discuss our views further in detail, please do not hesitate to contact us.

7

15 January 2010

Greg Tanzer
Secretary General
IOSCO General Secretariat
Calle Oquendo 12
28006 Madrid
Spain

**Public Comment on the
Transparency of Firms that Audit Public Companies: Consultation Report**

Dear Mr. Tanzer:

Ernst & Young Global Ltd., the central entity of the global Ernst & Young organization, welcomes the opportunity to offer our views on the consultation report on Transparency of Firms that Audit Public Companies issued by the International Organization of Securities Commissions in September 2009.

We agree with IOSCO that audit quality and the availability and delivery of audit services are critically important to investors and other stakeholders. High quality audits contribute to investor confidence in financial reporting. Investors should be able to rely on the accuracy of financial statements in order to help them make informed investment decisions.

Because audit firms play a vital role in enhancing investor confidence, greater investor understanding of audit work and the measures audit firms take to provide high quality audits could also help to bolster investor confidence in financial reporting. We understand that this led IOSCO to study whether enhancing the transparency of audit firms would serve to maintain or improve audit quality and the availability and delivery of audit services.

Audit firm transparency may not only be important to investors but also to audit oversight authorities and other stakeholders, including audit committees. However, these various stakeholder groups have differing information needs that should be taken into account when considering audit firm transparency. The type and extent of information disclosed, as well as the manner in which it is disclosed, is likely to vary, depending on which group of stakeholders is addressed.

We believe therefore that additional transparency disclosures require careful study and analysis to ensure they have the desired effect and are appropriate for a particular audience. In our view, the considerations should center on the following criteria:

- Is the additional disclosure relevant to understanding, maintaining or improving audit quality?
- Can the stakeholders to whom the additional disclosure is addressed understand it and is it relevant for them?
- Does the additional disclosure entail any risks or unintended adverse effects and what are the cost vs. benefits? (This assessment should include consideration of whether disclosure should be public or limited to confidential reporting to regulators.)

Furthermore, as it considers transparency disclosures, IOSCO should recognize the improvements that independent audit oversight has brought to audit quality in the last five years. In many ways, these independent audit oversight authorities stand in the shoes of investors and the public in order to protect their interests. To that end, through their oversight and inspections most oversight authorities are able to obtain an informed view into audit firms.

We believe that this level of transparency to our oversight authorities is particularly valuable and, indeed, should be extended around the world.

In this context, following the format of the Report, we would like to provide the following comments:

Possible Effects of Transparency Related to Audit Quality and Availability and Delivery of Audit Services

We agree with IOSCO that audit quality is difficult to define. However, we believe that it is not necessary to define audit quality in order to evaluate it, and that a reasonable alternative is to consider the attributes -- or indicators -- of audit quality. We believe that there are attributes, behaviours and indicators of audit quality that should be considered in addition to those referenced in the consultation report. Please refer to our discussion of potential audit quality indicators in the separate section below.

Transparency of Audit Firms' Governance

We believe that transparency disclosure regarding the way audit firms govern themselves and their commitment to audit quality can contribute to investor confidence in financial reporting and support informed decision making of all stakeholders.

With regard to whether there are areas of governance where additional disclosure should be considered, in our view Article 40 of the European Union's Statutory Audit Directive has

become a de facto benchmark for audit firm transparency reporting, including in the area of governance.

The Article 40 requirements include governance-related information such as a description of the firm's legal structure and ownership, a description of the network and the legal and structural arrangements in the network, a description of the governance structure of the audit firm, and a description of the internal quality control system of the audit firm. A number of Ernst & Young member firms have already published Article 40 transparency reports in a consistent format and with consistent content. We expect this number to grow as more EU Member States implement Article 40. In addition, the third country audit firm registration process will result in a number of audit firms outside the EU being required to publish Article 40 transparency reports.¹ We hope Article 40 transparency reporting will drive global consistency in transparency reporting and in this way improve the comparability of transparency disclosures in different countries. In addition, global consistency in reporting requirements could help make compliance with transparency requirements more cost efficient. We discuss the issue of consistency in more detail below.

Transparency of Audit Firms' Audit Quality Indicators

We believe that certain audit quality indicators, if carefully designed, could provide objective information to various audiences when evaluating a firm's audit quality. Such indicators could complement narrative disclosures, e.g., regarding an audit firm's quality control processes, which can over time become boilerplate, as pointed out on page 12 of IOSCO's consultation report.

Optimal indicators of audit quality (both input and output measures) should be designed to avoid unintended negative consequences, be high level and principle-based, and be limited to those that are truly indicative of audit quality. In our view, the following may be regarded as examples:

- Strength and consistency of the culture of an audit firm.
- Technical skills of audit partners and staff.
- Adherence to auditing standards.
- Existence and application of robust auditing processes.
- Compliance with Independence standards.
- Organization of auditor training and qualifications.

Disclosure of some of the above indicators may only be appropriate for disclosure to audit oversight authorities.

¹ In addition to the member firm transparency reports, Ernst & Young Global has published a voluntary global transparency report, which also includes a description of key elements of our governance framework

We would like to comment specifically on some of the additional disclosures discussed in the consultation report:

- Client dismissals, employee workload

Some additional disclosures may raise concerns with respect to protections under local laws which bar audit firms from making them. In our view, disclosures of client dismissals and employee workload, which are both discussed in the consultation report, are examples of additional disclosures which raise such concerns. Audit firms may be prohibited under local employment law from disclosing the workload of their employees. Applicable laws on client confidentiality may also prevent audit firms from disclosing to the public why they dismissed particular clients.

Moreover, in our view these disclosures are not likely to be equally relevant to all groups of stakeholders. Employee workload may be of particular interest for audit committees, as it may give them an indication of how much time each engagement team member will be able to spend on the audit. Disclosure of employee workload to audit committees may be much less problematic in certain jurisdictions than disclosure to the public. Furthermore, aside from the legal issues of disclosing details on the decision to dismiss an audit client, it may not be relevant to investors why an audit firm dismissed a particular audit client. However, this information may be relevant to the audit firm's oversight authority and disclosure to it under confidentiality may not raise legal issues. Therefore, as with all potential additional transparency reporting requirements, the nature of the reporting should take into account the intended audience.

- Pending Litigation

In our view, providing information on pending litigation is an example of a disclosure that may only be particularly relevant to a certain group of stakeholders, i.e., oversight authorities, and may have an unintended prejudicial effect with investors and the wider public.

In our experience, litigation may be complex and claims may be partly or wholly unfounded. In a confidential disclosure to oversight authorities we think it would be possible to explain the details of pending litigation and to put it in perspective. Such disclosure would meet the oversight authorities' interest in assessing the viability of audit firms while avoiding the adverse effects of a public disclosure.

It may be very difficult to explain this complexity adequately in a public disclosure, which will be relatively brief. There would be a risk of misunderstandings among investors about the severity of the matter disclosed which may lead investors to wrong conclusions about the viability of the audit firm in question. We are concerned that, rather than promoting audit quality, such disclosure may adversely and unfairly affect the public's confidence in the audit profession.

Transparency of Audit Firms' Financial Statements

Consistent with the criteria set forth above, we believe IOSCO should consider whether the disclosure of audit firms' financial statements would contribute to an understanding of audit quality. In this context, we think IOSCO should instead assess whether other financial information, such as for example the disclosure of fee income specified by audit services and non-audit services, as is already required by Article 40, would give investors and other stakeholders more meaningful information. That said, even that information may not be directly correlated to audit quality.

Moreover, we believe that considerations of public disclosures of audit firms' financial statements also should recognize the ongoing debate on the issue. While there are already some jurisdictions where disclosure of financial statements is required, the same may not be appropriate in every environment.

Parameters of Enhanced Disclosure for Audit Firms

We agree with the consultation report's conclusion that "additional transparency does not necessarily mean that everything has to be publicly disclosed". Rather, additional transparency requires careful consideration as to what piece of information is relevant for which group of stakeholders.

As the consultation report rightly points out, for example, the viability of an audit firm may be a primary concern for oversight authorities as they are concerned about the functioning of the audit profession as a whole, while audit committees may be more specifically concerned about whether an audit firm has the capacity to serve their companies.

As mentioned above, we believe that transparency to oversight authorities is particularly valuable. Over the last decade, independent oversight and regulation of auditors have played a key role in furthering the quality of our work and instilling public confidence in the profession. We support this oversight and the contributions it makes to enhancing audit quality. We appreciate that independent audit oversight authorities review our work and our systems of quality control. Therefore, we fully support transparency to our oversight authorities.

For good reasons much of the information disclosed to oversight authorities is subject to confidentiality and other protections afforded by applicable laws and regulations. We believe that these protections enable audit firms to be frank and open, thus facilitating a robust regulatory dialogue.

Consistency

In addition to the above described considerations, in our view, consistency of requirements is key to making transparency disclosures both effective and efficient. As set out above, we believe that consistency of transparency requirements across jurisdictions would make

the disclosures comparable and thus better understandable to investors and other stakeholders. It would also minimize duplicative costs for audit firms.

Conclusion

In conclusion, we believe that additional transparency disclosures may have a positive effect on audit quality if they are relevant to audit quality, are addressed to the right stakeholders and do not entail unintended adverse effects. Above all, transparency to our oversight authorities is key to audit quality and we fully support it.

We would be pleased to discuss our comments with IOSCO or its representatives at your convenience. Please send any correspondence for the attention of Trevor Faure, Global General Counsel (trevor.faure@uk.ey.com).

Yours sincerely,

Ernst & Young Global Ltd.

Greg Tanzer
Secretary General
IOSCO General Secretariat
Calle Oquendo 12
28006 Madrid
Spain

15th January 2010

Public Comment on the Transparency of Firms that Audit Public Companies: Consultation Report

FAR SRS, the Institute for the Accountancy Profession in Sweden, is responding to your request for consultation on the matters discussed in your Consultation Report on Transparency of Firms that Audit Public Companies.

FAR SRS fully supports FEE's response (see attachment) to the IOSCO consultation report.

FAR SRS



Anna-Clara af Ekenstam
*Chairman of FAR SRS section for
large entities*



Dan Brännström
Secretary General

Attachment: FEE response to IOSCO consultation



Federation of European Accountants
Fédération des Experts comptables Européens

Mr. Greg Tanzer
Secretary General
IOSCO General Secretariat
Calle Oquendo 12
28006 Madrid
Spain

auditorcommunications@iosco.org

13 January 2010

Ref.: AUD/HvD/LA/SH

Dear Mr. Tanzer,

Re: FEE Comments on the IOSCO Technical Committee Consultation on the Transparency of Firms that Audit Public Companies

FEE (the Federation of European Accountants) is pleased to provide you below with its comments on the Technical Committee of the International Organization of Securities Commissions (IOSCO) Consultation on Transparency of Firms that Audit Public Companies (the IOSCO Consultation Paper or the Consultation Paper).

FEE welcomes the debate on transparency of firms that audit public companies which has attracted the attention of a variety of stakeholders around the globe. The IOSCO Consultation Paper is one of the contributions to this global debate, in addition to the views of investors, issuers, preparers, regulators, legislators and auditors. FEE strongly believes that all these stakeholders should work together to improve communication to investors without any particular stakeholder taking this debate forward unilaterally. FEE would therefore recommend that IOSCO publishes the responses received to this Consultation Paper, as well as a summary thereof to aid transparency towards all stakeholders concerned.

Audits of financial statements are carried out in the public interest. In order for users of financial statements to understand this contribution to the public interest, transparency of those charged with audits is desirable. FEE is therefore supportive of transparency of audit firms as this should contribute to ensuring that audits of financial statements are carried out in the public interest.

As representatives of the European audit profession, FEE constantly contributes to promoting high quality audits. FEE is therefore supportive of public oversight of the audit profession and audit firms as FEE believes that public oversight contributes to enhancing audit quality.

Our main comments to the IOSCO Consultation Paper are summarised below:

- (1) In the European Union, the requirements in respect of transparency of auditors of public interest entities are set out in the Statutory Audit Directive¹ as implemented in the European Union .
- (2) FEE refers to Article 40 on 'Transparency reports' of the Statutory Audit Directive which requires for auditors of public interest entities that an annual transparency report is published which includes comprehensive information related to governance of the audit firm. The disclosures required in Article 40 are mainly a description of the legal structure, the ownership and the governance structure of the audit firm, a description of any network that the audit firm belongs to and a description of the internal quality control system of the audit firm. FEE believes that the information provided in such transparency reports ensures a high level of transparency for audit firms of public interest entities.
- (3) The Statutory Audit Directive strives to achieve high quality audits and therefore Article 26 of the Statutory Audit Directive requires audits to be carried out on the basis of international auditing standards.
- (4) Article 26 of the Statutory Audit Directive on 'Auditing standards' gives authority to the European Commission to adopt international auditing standards for all statutory audits in the European Union. International Standards on Auditing (ISAs) as issued by the International Auditing and Assurance Standards Board (IAASB) are already commonly used to perform audits in European Union Member States². In June 2009, the European Commission issued a Consultation Paper proposing to adopt the ISAs. It is expected that such adoption will effectively be announced and take place in the near future.
- (5) This demonstrates that the Statutory Audit Directive is a legal instrument which deals with and links both transparency of audit firms, auditing public interest entities and audit quality. FEE is of the view that the requirements, experiences and results of the European regulation regarding transparency and audit quality are relevant for consideration at an international level.

Our detailed comments and responses to the questions set out in the IOSCO Consultation Paper are included in the Appendix attached hereafter and centre on matters of principle that are of relevance to the European accountancy profession as a whole and are not formed from the viewpoint of investors.

¹ <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2006:157:0087:0107:EN:PDF>

² http://ec.europa.eu/internal_market/consultations/docs/2009/isa/consultation_ISAs_en.doc

For further information on this FEE³ letter, please contact Mrs. Hilde Blomme at +32 2 285 40 77 or via email at hilde.blomme@fee.be from the FEE Secretariat.

Yours sincerely,



Hans van Damme
President

³ FEE is the Fédération des Experts comptables Européens (Federation of European Accountants). It represents 43 professional institutes of accountants and auditors from 32 European countries, including all of the 27 European Union (EU) Member States. In representing the European accountancy profession, FEE recognises the public interest. It has a combined membership of more than 500.000 professional accountants, working in different capacities in public practice, small and big firms, government and education, who all contribute to a more efficient, transparent and sustainable European economy.

FEE's objectives are:

- To promote and advance the interests of the European accountancy profession in the broadest sense recognising the public interest in the work of the profession;
- To work towards the enhancement, harmonisation and liberalisation of the practice and regulation of accountancy, statutory audit and financial reporting in Europe in both the public and private sector, taking account of developments at a worldwide level and, where necessary, promoting and defending specific European interests;
- To promote co-operation among the professional accountancy bodies in Europe in relation to issues of common interest in both the public and private sector;
- To identify developments that may have an impact on the practice of accountancy, statutory audit and financial reporting at an early stage, to advise Member Bodies of such developments and, in conjunction with Member Bodies, to seek to influence the outcome;
- To be the sole representative and consultative organisation of the European accountancy profession in relation to the EU institutions;
- To represent the European accountancy profession at the international level.

Appendix – Detailed comments

This appendix contains FEEs detailed comments and responses to the questions set out in the IOSCO Consultation Paper.

1. Is a definition of audit quality necessary to evaluate audit quality or can audit quality be evaluated from an understanding of the attributes, behaviors, and indicators of audit quality?

Measurability of audit quality

- (1) FEE welcomes the debate in relation to audit quality as addressed by IOSCO. FEE would like to caution that defining and measuring audit quality might not be straightforward or even possible. Some organisations have invested significant resources to identify indicators, characteristics or features of audit quality, like the UK Audit Quality Forum⁴. However, such indicators are not considered to be comprehensive enough to form the basis for a common set of indicators to compare audit quality or for a definition of audit quality as judgement will have to be used when considering audit quality.
- (2) Additionally, depending on the legal, regulatory, professional, regional, cultural and other circumstances, assessments of audit quality might differ. That is why a workable definition of audit quality seems to be extremely challenging, if not impossible to achieve. Additionally, the evaluation of audit quality is likely to differ depending on the perspective from which audit quality is assessed because regulators and investors may have different perception of, and thus criteria for, such an evaluation.

Statutory Audit Directive

- (3) The European Union Statutory Audit Directive aims at ensuring consistently high quality in all statutory audits required by European Community law. This is achieved by regulating all aspects of an audit including as most important ones the education of auditors, their ethics and independence, auditing standards to be used as well as audit reporting, quality assurance of auditors, investigations and penalties for auditors and the public oversight of auditors.
- (4) No common definition for audit quality is included in the Statutory Audit Directive as all aspects pertaining to an audit as indicated above are believed to contribute to high quality auditing.

⁴

http://www.icaew.com/index.cfm/route/155421/icaew_ga/en/Technical_and_Business_Topics/Thought_leadership/Audit_Quality_Forum/Audit_Quality_Forum

Appendix – Detailed comments

- (5) FEE is therefore of the view that the effects for European audits and audit firms of the requirements, experiences and results of the implementation of the Statutory Audit Directive in the European Union should be analysed before deciding on any further initiatives on international level.

IAASB

- (6) The IAASB has initiated a project on 'Addressing the Expectation Gap on Audit Quality' as announced in the IAASB Strategy and Work Program 2009-2011. This project has commenced and a first discussion took place in the IAASB Board meeting in December 2009⁵. FEE welcomes this initiative taken by the IAASB and would therefore recommend to await the results of the IAASB project before considering any further initiatives in respect of defining audit quality.

- (7) Currently, the ISAs do not include any definition of audit quality. ISAs are currently applied in the majority of the European countries and in well over one hundred countries worldwide as it is widely accepted that applying ISAs results in high quality audits.

2. In addition to competence and industry expertise of the audit personnel, firm culture that promotes audit quality, firm-wide quality control systems, and auditor oversight, are there other examples of attributes, behavior, and indicators of audit quality that should be considered?

- (8) The indicators selected in question 2 are competence, culture, quality control and oversight, but depending on the sources consulted, there are other indicators or attributes of audit quality which could have been identified and selected.
- (9) The legal, regulatory and professional environment in which professional accountants work include amongst other things ethical and quality requirements which follow from the code of ethics for professional accountants, the Statutory Audit and Transparency Directives, the International Standard on Quality Control (ISQC) 1 and internal and external quality assurance systems.

⁵ <http://www.ifac.org/IAASB/Meeting-BGPapers.php?MID=0169&ViewCat=1196>

Appendix – Detailed comments

(10) The following should also be considered:

- (a) There are five fundamental principles (integrity, objectivity, professional competence and due care, confidentiality, professional behaviour) set out in the International Ethics Standards Board for Accountants (IESBA) Code of Ethics for Professional Accountants⁶ and partly in the Statutory Audit Directive. All these fundamental principles should be applied and ethics covered in the consultation paper as competence, culture, quality control and oversight is therefore not the only fundamental principle that is relevant for professional accountants.
- (b) Other elements of a system of quality control (leadership, relevant ethical requirements, acceptance and continuance of client relationships, human resources, engagement performance, monitoring) of International Standard on Quality Control 1⁷ (ISQC 1) could also be considered.
- (c) The Statutory Audit Directive contains other aspects that could also be considered. These other aspects could be approval of statutory auditors, continuing education and mutual recognition; registration; professional secrecy; auditing standards and audit reporting; (external) quality assurance; investigations and penalties; public oversight; public interest entities, etc.

(11) FEE would therefore recommend that the aspects addressed in this question are broadened out to cover these additional aspects of ethics for professional accountants.

3. Are there other areas of governance for which additional transparency should be considered?

(12) Reference is made to Article 40 of the Statutory Audit Directive on 'Transparency reports' which requires for auditors of public interest entities that an annual transparency report is published⁸. FEE is of the view that the information

⁶ <http://www.ifac.org/Members/Downloads/code-of-ethics-for-professi-2.pdf>

⁷ http://web.ifac.org/download/2009_Auditing_Handbook_A007_ISQC_1.pdf

⁸ Article 40 requires that a transparency report includes at least

- (a) A description of the legal structure and ownership;
- (b) Where the audit firm belongs to a network, a description of the network and the legal and structural arrangements in the network;
- (c) A description of the governance structure of the audit firm;
- (d) A description of the internal quality control system of the audit firm and a statement by the administrative or management body on the effectiveness of its functioning;
- (e) An indication of when the last quality assurance review referred to in Article 29 took place;
- (f) A list of public-interest entities for which the audit firm has carried out statutory audits during the preceding financial year;
- (g) A statement concerning the audit firm's independence practices which also confirms that an internal review of independence compliance has been conducted;
- (h) A statement on the policy followed by the audit firm concerning the continuing education of statutory auditors referred to in Article 13;

Appendix – Detailed comments

provided in such transparency reports ensures a high level of transparency for audit firms of public interest entities and does therefore not see a need to add further disclosures.

- (13) The disclosures required in Article 40 are mainly a description of the legal structure, the ownership and the governance structure of the audit firm, a description of any network that the audit firm belongs to and a description of the internal quality control system of the audit firm.
- (14) Article 40 forms the basis of transparency disclosures for EU audit firms auditing public interest entities which are entities governed by the law of a Member State whose transferable securities are admitted to trading on a regulated market of any Member State.
- (15) As the scope of Article 40 of the Statutory Audit Directive and the IOSCO Consultation Paper is the same, FEE believes that the information provided in such transparency reports in accordance with Article 40 of the Statutory Audit Directive ensures a high level of transparency for audit firms auditing public interest entities.
- (16) As far as external quality assurance or inspections are concerned, the 2008 European Commission Recommendation on Quality Assurance requires certain disclosures related to the outcome of inspections, like the public disclosure of major deficiencies in internal quality control systems and of disciplinary actions taken or penalties imposed, apart from other disclosures to the audit firm under inspection.
- (17) It should also be noted that Article 41 of the Statutory Audit Directive on 'audit committees' assigns certain monitoring and review responsibilities to the audit committee of public interest entities, which results in a number of areas of governance for which no public transparency but transparency to those charged with governance is considered appropriate.

(i) Financial information showing the importance of the audit firm, such as the total turnover divided into fees from the statutory audit of annual and consolidated accounts, and fees charged for other assurance services, tax advisory services and other non-audit services;

(j) Information concerning the basis for the partners' remuneration.

Appendix – Detailed comments

4. *Would the proposed disclosures mentioned above be useful in improving audit quality and availability and delivery of audit services to public companies?*

(18) It is perceived that audit quality is already at a high level although further improvements in certain aspects of audit quality could be considered which is also under consideration by the IAASB in relation to its current project on Audit Quality as mentioned in our response to question 1.

(19) The Statutory Audit Directive had to be implemented in EU Member States by mid 2008. The assessment of the effectiveness of the transparency disclosures required in article 40 of the Statutory Audit Directive is therefore limited and further experience should be awaited. At this stage, FEE is of the view that the Articles 40 and 41 requirements in the Statutory Audit Directive regarding transparency disclosures and audit committees ensure a high level of transparency for audit firms of public interest entities as mentioned in the response to question 3.

5. *Could other limitations arise if such disclosures were required?*

(20) Item (f) of Article 40 in the Statutory Audit Directive states that *“a list of public-interest entities for which the audit firm has carried out statutory audits during the preceding financial year”*.

(21) Additionally, Article 40 of the Statutory Audit Directive permits EU Member States not to apply the requirements of Article 40 (f) in exceptional circumstances if necessary to mitigate an imminent and significant threat to the personal security of any person. Any information which forms such or a similar threat like to personal or commercial privacy of information should be limited for disclosure purposes following the ‘comply or explain’ approach.

(22) Given the level of detail proposed, comparability is likely to be impaired and, furthermore, there is a risk for a significant information overload in case all information discussed in the Consultation Paper were disclosed publicly.

6. *Can audit quality indicators provide objective information when evaluating a firm’s audit quality. If so, do the ones identified in this report accomplish that goal?*

(23) As mentioned in the responses to questions 1 and 2 FEE is of the view that other audit quality indicators should be taken into consideration and that all indicators together can not be considered to be comprehensive enough to form the basis for a common set of indicators to compare audit quality or for a definition of audit quality. Reference is made to our responses to these questions.

Appendix – Detailed comments

(24) In addition, FEE would like to highlight that the use of professional judgement is crucial in performing audits and in assessing audit quality. Professional judgement has to be applied to respond to inherent limitations to obtaining objective information when evaluating audit quality. It is clear that objectivity should be part of the assessment of the effectiveness of quality control systems but judgement will have to be used when performing such an assessment.

7. In addition to the indicators identified in this report, are there any other audit quality indicators that should be considered for disclosure? Would disclosure of the audit quality indicator described above be helpful in evaluating audit quality?

(25) As mentioned in the responses to questions 1 and 2 FEE is of the view that other audit quality indicators should be taken into consideration. Reference is made to our responses to these questions.

(26) We would however like to comment on a few particular disclosure proposals made in the IOSCO Consultation Paper:

(a) In section C on page 16, disclosures on insurance coverage are referred to as information that may improve both audit quality and the availability and delivery of audit services. Such information is currently not explicitly required to be disclosed under the Statutory Audit Directive.

FEE is of the view that if disclosures on insurance coverage would ever be required, only a clear statement that the audit firm has insurance coverage would be relevant. Information about the premium of the insurance coverage is in FEE's view not relevant for the transparency of audit firms regarding audit quality.

(b) In section D on page 16, restatements of financial statements are referred to as an indicator of audit quality. FEE would like to highlight that legislation in various jurisdictions restricts the ability to restate financial statements. Therefore, the number of restatements can hardly be a relevant indicator of audit quality which contributes to increased transparency about audit quality.

(c) In section E on page 17, client acceptance and dismissal information is referred to as an indicator of audit quality. Article 38 of the Statutory Audit Directive does not require public disclosure of dismissals and resignations of audit firms but that public oversight authorities are informed about dismissals or resignations during the term of appointment and are given an adequate explanation of the reasons therefore. FEE is of the opinion that further public disclosures might go too far and might violate privacy laws and regulations in a number of jurisdictions.

Appendix – Detailed comments

8. *In addition to the benefits or limitations identified in this report, are there any other benefits or limitations about disclosing audit quality indicators that need to be considered?*

(27) FEE does not have any further comments in this regard.

9. *Can audited financial statements of audit firms provide useful or objective information regarding audit quality? If so, how?*

(28) Audited financial statements are usually considered as a measure to enhance transparency of the audited entity and as a sign of good governance. This will apply regardless of whether the audited entity is an audit firm or not. Whether or not the financial statements, in case the audited entity is an audit firm, provide useful and/or objective information regarding the quality of the audits performed by the audit firm is not necessarily clear-cut and is not necessarily the purpose of the financial statements of an audit firm.

(29) The financial statements for an audit firm, like for any other company, can demonstrate whether the business itself is financially sound. For audit firms, in particular, financial statements are a means to demonstrate whether the audit firm has a proper and sound financing structure as financial stability is a prerequisite, but only a prerequisite, for the 'business model' of an audit firm.

10. *If disclosure to the public or regulators of an audit firm's own audited financial statements is warranted, who should audit the auditors? Are firms other than the Big Four equipped to audit the Big Four? If not, does having the Big Four firms audit each other raise concerns? If so, how could any such concerns be addressed?*

(30) In general, the audit of an audit firm is not excessively complicated and the financial statements of an audit firm can thus be audited by any audit firm. The complexity of an audit firm appears mainly in the consultancy departments of an audit firm where longer term projects and assessment of work in progress are important. The auditor of an audit firm will need to carry out risk assessment procedures and assess the professional competence and knowledge of the business model in the same way as for any audit client in any line of business.

(31) The practice of whether big four audit firms audit each other varies across Europe as in some countries big four audit firms are audited by another big four audit firm whilst this is not the case in other countries. As for any other audit client an audit firm accepts, it has to assess the threats to its independence in accordance with the independence requirements in the Statutory Audit Directive. If independence is threatened, safeguards have to be applied and if no safeguards can eliminate or reduce the threats to an insignificant level, the auditor should not carry out the audit. These principles apply in all situations

Appendix – Detailed comments

where audits are carried out and therefore also in a situation where the audited entity is an audit firm. FEE is of the view that these principles are sufficient for the auditors to assess the threats and the safeguards that need to be in place when auditing an audit firm.

- (32) Because of independence requirements and conflicts of interest, it can be difficult for big four audit firms to audit each other. Indeed, because of prohibitions on the provision of non-audit services to audit clients, different big four audit firms often have the same public interest entities as clients, one as an audit client and others as clients for the provision of non-audit services. In practice, it appears that smaller audit firms are more likely to have no such independence conflicts.

11. Can disclosing certain financial information instead of audited financial statements achieve the same objective of improving audit quality and the availability and delivery of audit services? If so, what financial information should be disclosed?

- (33) We refer to our response to question 9. FEE is of the view that financial information included in audited financial statements for audit firms, prepared in accordance with the legislative requirements for financial statements, together with the financial information in the transparency report following Article 40 of the Statutory Audit Directive, ensure a high level of transparency for audit firms of public interest entities. Therefore, no additional requirements setting out new disclosures for audit firms should be introduced.

12. Are there other parameters that should be considered?

- (34) FEE is of the view no other parameters would be relevant to consider.

13. Should certain disclosures not be publicly available and if so, what criteria should be considered when determining what disclosures should be publicly available?

- (35) FEE agrees that different stakeholders have different information needs. Not all information about an audit firm is relevant for all users of financial statements. For instance, under the Statutory Audit Directive comprehensive information is submitted by the audit firms to the audit public oversight authorities. Such information is submitted as part of the inspection process or external quality assurance reviews of the audit firm in question. This information is relevant to the public oversight authorities, but not necessarily to users of financial statements audited by the audit firm in question.

Appendix – Detailed comments

- (36) FEE also agrees that the role of a securities regulator is to protect investors and to ensure that investors are provided with all relevant and necessary information in order to make informed investment decisions. Other regulators have other roles. Audit regulators have to ensure the quality of the audits carried out. This entails that information submitted to the audit public oversight authorities would not necessarily have the same level of relevance to the securities regulator in their role of investor protection as it has for the audit regulator in its role of protecting audit quality. Information about audit inspections should therefore not necessarily be shared with securities regulators although the information has relevance for the audit public oversight authorities.
- (37) Another example of different information needs could be the role of audit committees. In accordance with Article 41 of the Statutory Audit Directive, audit committees are provided with information that would not necessarily be relevant for investors in a broader context.
- (38) FEE is therefore of the view that situations could occur where certain disclosures would and should not be publicly available.

14. Should certain disclosures be made at the network, firm, and/or, engagement level?

- (39) In general, the level at which information is disclosed, whether it is network, firm, office or engagement levels, will depend on the type of information considered for disclosure on a case-by-case basis. In addition, with the aim of increasing transparency of the audit firm some networks provide additional information about the network on their websites.
- (40) However, as mentioned in the response to question 3, Article 40 of the Statutory Audit Directive requires that comprehensive information be disclosed by audit firms of public interest entities. FEE believes that these transparency reports strike a good balance as far as disclosing information which is relevant for users of financial statements. Therefore, FEE does not see a need for additional disclosures made at network, firm or engagement level.

15. Should there be different disclosure requirements for large, mid-size, and small audit firms?

- (41) In line with Article 40 of the Statutory Audit Directive, disclosure requirements set out in the transparency report appear most appropriate for audit firms auditing public interest entities regardless of whether the audit firm is a large, mid-size or small audit firm.

Appendix – Detailed comments

(42) Additional disclosures related to the size of the audit firm should be carefully considered and a thorough cost-benefit analysis should be conducted prior to introducing additional disclosures along these lines. It should also be taken into consideration that being a large, mid-size and small audit firm can vary from one country to another, even if the national audit firms belongs to the same network at international level.

(43) Introduction of additional governance initiatives could create obstacles for mid-size or smaller audit firms to enter the audit market of public interest entities thereby furthering concentration in the audit market. FEE is of the view that striving to increase transparency of audit firms should not result in perpetuating market concentration.

16. Should the disclosures be mandatory and if so, should they be subject to regulatory oversight? Would a similar impact to the markets occur if the disclosures were encouraged instead of being mandatory? Should consideration be given to a framework of audit quality and allow for flexibility in the types of disclosures?

(44) In line with our previous responses, we believe that disclosure similar to the ones required by Article 40 of the Statutory Audit Directive could be made mandatory for audit firms auditing public interest entities. The public oversight of Article 40 on transparency reports is to be assumed by national audit oversight authorities. Although we are not of the opinion that there is currently a need for additional disclosures, any such additional disclosures should preferably be provided on a voluntary basis, following the ‘comply or explain’ principle.

(45) In this respect, reference is made to the FEE Comments on the Second ICAEW/FRC Consultation Paper on Audit Firm Governance⁹, which commented on the following:

We see a risk of overregulation and an increase of bureaucratic burdens in Europe if further disclosure requirements beyond the Statutory Audit Directive and the EC Recommendations are considered, given the public oversight systems already in place. We think there would be benefits in understanding how the different current requirements are being implemented in European Union Member States, particularly with regard to transparency reports and independence before considering additional regulatory measures.

⁹

<http://www.fee.be/fileupload/upload/Hodgkinson%20091010%202nd%20Consultation%20Paper%20Audit%20Firm%20Governance1210200951620.pdf>

Appendix – Detailed comments

In general the expected benefits of disclosures brought by a further improvement of governance practices are for example related to enhanced dialogue between auditors and the shareholders and other stakeholders of listed companies. There is a potential risk that the compliance costs associated with additional disclosures will form a further barrier, in addition to the requirements imposed by the Statutory Audit Directive, especially for smaller audit firms. Therefore, we recommend including the size of the audit firm itself as an additional criterion if disclosures were to be mandatory.

17. Would transparency of audit firms improve audit quality and the availability and delivery of audit services? What negative effects, including costs, of increased transparency should regulators consider?

(46) As mentioned in the response to question 15 and 16 in the IOSCO Consultation Paper FEE is of the view that the benefits of additional transparency disclosures, especially for smaller audit firms, is not likely to outweigh the costs of providing them and the risk of increasing market concentration for audit firms.

18. Would investors have increased confidence in financial reporting as a result of increased audit firm transparency?

(47) Not applicable.

19. Are there significant benefits to investors of increased audit firm transparency, since they invest in companies and not audit firms?

(48) Not applicable.

20. Should regulators consider areas outside of audit firms' governance, audit quality indicators, and financial statements for potential disclosures?

(49) As mentioned in the response to question 3, Article 40 of the Statutory Audit Directive requires comprehensive information disclosed by audit firms of public interest entities. FEE believes that these transparency reports in accordance with Article 40 of the Statutory Audit Directive strike a good balance as far as disclosing information. Therefore, FEE does not see a need for additional disclosures made at network, firm or engagement level.



Financial Reporting Council

Aldwych House, 71-91 Aldwych, London WC2B 4HN

Telephone: 020 7492 2300 Fax: 020 7492 2301

www.frc.org.uk

Chairman: Sir Christopher Hogg

Chief Executive: Stephen Haddrill

Company Secretary: Anne McArthur

Mr G Tanzer Esq
Secretary General
IOSCO General Secretariat
Calle Oquendo 12
28006 Madrid
Spain

22 December 2009

Dear Mr Tanzer

Transparency of Firms that Audit Public Companies

The Financial Reporting Council (FRC) is the United Kingdom's independent regulator responsible for promoting confidence in corporate reporting and governance.

The FRC is pleased to note that IOSCO is consulting on this important issue, as we believe that increased transparency is an important driver of audit quality. Further details on this are below. We would also comment that it seems contradictory that auditors, whose role helps to ensure appropriate transparency of their clients, should be less transparent themselves.

Our comments on the issues raised by the consultation document are below. Given the publications on transparency issued by the FRC of which we know you are familiar, we have kept our comments at a high level. Please do not hesitate to contact us if you would like clarification on any particular point.

1 Audit quality

Our overriding point is that transparency reports provide an opportunity for firms to compete on quality. Audit firms and those that use their services should not miss this opportunity and therefore transparency reports should not become boilerplate but should provide an appropriate framework for firms to distinguish themselves from their competitors on this basis of quality. This in turn requires a greater understanding of audit quality.

There is no single definition of audit quality. However there are a number of drivers and indicators which are likely to contribute to audit quality. The consultation document picks up most of the main indicators of audit quality; we would add to those already mentioned the personal qualities of audit personnel and professional obligations to comply with ethical codes.

In 2008 the FRC published the 'Audit Quality Framework'. The Framework identified the following drivers of audit quality:

- The culture within an audit firm;
- The skills and personal qualities of audit partners and staff;
- The effectiveness of the audit process;
- The reliability and usefulness of audit reporting; and
- Factors outside the audit affecting audit quality.

The Framework is intended to assist audit firms, listed companies, investors, regulators and other stakeholders in understanding and assessing audit quality. Inevitably, however, many of these indicators are subjective. We accept that it is difficult to develop a set of objective metrics to measure all aspects of audit quality, but there are opportunities for identifying proxies to audit quality. In developing such proxies it is clearly necessary to guard against unintended consequences. The content and extent of a firm's disclosures on these issues should provide some indication of its attitude to these aspects of audit quality.

2 Transparency of audit firms' governance

The consultation document contains a comprehensive summary of the main audit firm governance arrangements which could be subject to enhanced transparency disclosures. We highlight in particular the issues around global networks, which are often exempt from national disclosure requirements and have opaque governance structures. There is a need for further work and analysis on this issue.

The question of transparency of audit firms' governance arrangements may also be linked to the ownership debate. An audit firm which was listed on a regulated exchange would be considered a public interest entity and would in most jurisdictions be subject to the same governance and transparency requirements as other large corporate bodies.

In 2006 the FRC established a Market Participants Group (MPG) to advise on possible actions which could be taken to mitigate the risks arising from concentration in the audit market for large public interest entities. The MPG published fifteen recommendations in October 2007, one of which was that 'every firm that audits public interest entities should comply with the provisions of a Combined Code-style best practice governance guide or give a considered explanation'.

Following this recommendation, the ICAEW established at the request of the FRC a working group to develop such a code for the governance of audit firms. A draft code has now been published and is expected to be finalised in the New Year.

3 Disclosure parameters

As noted in the consultation document, the European Union has through the Statutory Audit Directive set out a benchmark which could be used as a base for a global standard. The UK has fully implemented the Directive.

Under the UK's implementation of the Directive, only those firms with one or more audit clients with securities admitted to trading on a UK regulated market are required to publish transparency reports. We would consider this to be an appropriate level for mandatory disclosure as it does not place undue burdens on smaller firms. However, smaller firms could be encouraged to follow aspects of the guidance on a voluntary basis if by doing so they were able to improve their competitive position.

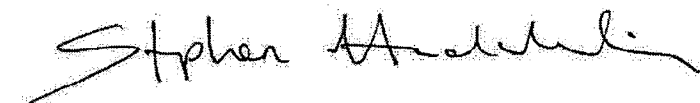
The consultation document asks whether certain disclosures should not be publicly available and what criteria may be used to determine when limiting disclosure in this way is appropriate. We believe that in some cases limited disclosure may be appropriate, for example a regulator's findings in respect of a particular audit and similar situations which are specific to an individual client. Client-specific matters which result in a finding of misconduct against an auditor should of course be made public, along with details of any regulatory sanction imposed.

4 Conclusion

In conclusion, the FRC believes that enhanced transparency reporting by audit firms is likely to strengthen audit quality. If done well, it provides a platform for auditors to compete on quality.

If you would like to discuss any of the comments made, then please contact Paul George on 020 7492 2340.

Yours sincerely



Stephen Haddrill

Chief Executive

DDI: 020 7492 2390

Email: s.haddrill@frc.org.uk

Mr Greg Tanzer
Secretary General
IOSCO General Secretariat
Calle Oquendo 12
28006 Madrid
Spain

Grant Thornton International Ltd
Regent's Place, 7th Floor
338 Euston Road
London NW1 3BG
United Kingdom
T +44 (0)20 7391 9500
F +44 (0)20 7391 9501
www.gti.org

15 January 2010

Dear Mr Tanzer

Public Comment on the Transparency of Firms that Audit Public Companies: Consultation Report

Grant Thornton International Ltd (Grant Thornton) welcomes the opportunity to comment on the above-referenced consultation report. Below we provide a number of general comments on the consultation paper, and in the appendix hereto we answer the specific questions posed.

Grant Thornton supports transparency that enhances an understanding of the audit process and audit quality

Audit quality is important for investor confidence in financial reporting, and Grant Thornton supports disclosures that enhance the understanding of the audit process and audit quality. As the consultation paper notes, regulators around the world already require certain disclosures, both publicly to investors and confidentially to regulators, of audit firms in their jurisdictions.

To this end, we believe the capital markets would benefit if regulators were to adopt consistent audit firm transparency and disclosure requirements in their respective jurisdictions. Consistency with respect to transparency requirements would help stakeholders better understand the disclosures. It could also lead to mutual reliance, whereby regulators could rely on their counterparts in an audit firm's home country for primary oversight of those audit firms.

Grant Thornton supports public disclosure of balanced inspection reports
Grant Thornton supports the publication of fair and balanced results of audit inspections of individual audit firms. We believe that a rigorous inspection process is important for supporting market confidence in audit quality, and the public disclosure of fair and balanced inspection reports could enhance the public's knowledge about audit firms and help drive audit quality.

In jurisdictions where inspection reports on individual firms are published, we believe that regulators should put their inspection results in context (focusing on both the positive and negative), and should present balanced inspection results with greater prominence. Doing so would better allow audit committees, and others involved in auditor appointment and re-

appointment, to make decisions based on independent assessments of audit quality rather than on perception.

As discussed below, we believe that audit firms would necessarily disclose more information confidentially to audit regulators than they should be required to disclose publicly. The publication of balanced inspection reports appropriately bridges the gap between confidential disclosures to audit regulators and disclosures to the general public. Public disclosure of audit firm inspection reports provides the public with, in essence, the same information that is provided to regulators, but it is in the form of the audit regulators' conclusions, which are based on their consideration of numerous confidential disclosures, as well as on their expert analysis of those disclosures.

Grant Thornton supports distinguishing between public and private disclosures

The consultation paper focuses upon whether audit firms should make some disclosures to the public at large and other disclosures confidentially to their audit or securities regulator. The distinction between public and confidential disclosure is critical. Investors and regulators are two very different constituencies in the financial reporting process, and each has a distinct role and distinct information needs.

Extensive confidential disclosures to audit oversight entities

Independent audit oversight entities seek to protect investors and the public interest by enhancing and promoting audit quality, and they help ensure the public's confidence in financial reporting. Audit oversight entities require audit firms to register and provide certain information as part of that registration, and they also require significant additional information of audit firms when conducting inspections of those audit firms.

Grant Thornton supports the role of audit oversight entities because independent oversight enhances audit quality and public confidence in financial reporting. The member firms of Grant Thornton are in fact highly transparent to their audit oversight entities. To the best of our knowledge, our member firms already provide to regulators a great deal of the information described in sections III and IV of the consultation paper.

Because audit oversight entities serve to promote audit quality, we support providing them with a wide array of information so they can properly assess audit quality. Proper assessment requires that audit oversight entities have the expertise necessary to understand a variety of disclosures — disclosures that might be significantly misunderstood by the public at large.

Importantly, much of the information provided by audit firms to their regulators as part of the inspection process is confidential and often privileged from legal disclosure. These protections against public disclosure are important because they help foster an open dialogue between audit firms and regulators, which in turn contributes to effective oversight and enhances audit quality.

Additional public disclosures to all stakeholders

Grant Thornton also supports providing certain transparency disclosures to the public because we believe that such disclosures can contribute to investor confidence in the financial reporting process. However, investors play a different role in the financial reporting process than do regulators. Investors' focus, and their expertise, is primarily with

respect to the company, not the audit firm. While investors must be reasonably assured of the quality of the audit, this assurance comes primarily from the independent audit oversight system, and in some jurisdictions from the local professional body where no independent regulator exists.

We therefore believe that disclosures provided to the public should be narrower than those provided to audit oversight entities. Wider disclosure of the types of sensitive information typically provided to audit oversight entities could lead to negative consequences, as discussed in the appendix to this letter, without an increase in audit quality.

As to which disclosures should be made public, we believe those required by Article 40 of the European Union's 8th Company Law Directive are appropriate. Many individual audit firms within the European Union have published transparency reports as required by Article 40, and many more will do so in the near future as EU Member States fully transpose the 8th Directive. Further, Grant Thornton has voluntarily published network transparency reports (see <http://www.gti.org/Transparency-report/index.asp>) that are modelled on the requirements of Article 40. We believe that regulators should analyse the effectiveness of the disclosures required by the recently-implemented Article 40 before requiring disclosures that go beyond Article 40.

We recognise that many of the disclosures required by Article 40 are governance-type disclosures described in section III of the consultation paper, and are not "audit quality indicators." At this point, we believe that very careful consideration should be given to requiring disclosures beyond those set forth in Article 40, particularly those described in section IV of the paper. There is inherent difficulty in identifying key indicators and drivers of audit quality, and there are negative consequences (discussed below) of wider public disclosure of the types of information set forth in section IV of the paper.

* * *

Appended to this letter are our responses to the questions posed in the consultation paper. If you have any questions, please contact April Mackenzie (phone: +1 212 542 9789; email: April.Mackenzie@gt.com), Jon Block (phone: +1 202 861 4100; email: Jon.Block@gt.com), or Nick Jeffrey (phone: +44 207 728 2787; email: Nick.Jeffrey@gtuk.com).

Yours faithfully



April Mackenzie
Global head - public policy and external affairs
Grant Thornton International Ltd
Direct T: +1 212 542 9789
E: April.Mackenzie@gt.com

Appendix – Consultation Questions

Possible effects of transparency related to audit quality and availability and delivery of audit services

Question 1: *Is a definition of audit quality necessary to evaluate audit quality or can audit quality be evaluated from an understanding of the attributes, behaviors, and indicators of audit quality?*

Grant Thornton response: We believe that establishing an abstract definition would contribute little to evaluating audit quality. We believe that audit quality can be evaluated by an understanding of the attributes, behaviours and indicators of audit quality, but in practice we believe that it is difficult to determine specific disclosures that will adequately measure these attributes, behaviours and indicators.

Question 2: *In addition to competence and industry expertise of the audit personnel, firm culture that promotes audit quality, firm-wide quality control systems, and auditor oversight, are there other examples of attributes, behaviours, and indicators of audit quality that should be considered?*

Grant Thornton response: Grant Thornton believes that any discussion of audit quality should begin with International Standard on Quality Control 1 (ISQC1), as issued by the International Auditing and Assurance Standards Board (IAASB). ISQC1 concerns an audit firm's responsibilities for its system of quality control, and it requires firms to establish and maintain a system of quality control that includes a number of specific elements, such as: leadership responsibilities for quality; ethical requirements; acceptance and continuance of client relationships and specific engagements; human resources; engagement performance; and monitoring. The assessment of regulators as to whether an audit firm has met the requirements of ISQC1 is a critical element in helping to promote audit quality.

Transparency of audit firms' governance

Question 3: *Are there other areas of governance for which additional transparency should be considered?*

Grant Thornton response: We believe the areas covered in the consultation paper are sufficient. With respect to which audit firm governance disclosures should be required, we suggest that regulators focus on those required by Article 40 of the European Union's 8th Company Law Directive, for the reasons stated in the body of our comment letter.

Question 4: *Would the proposed disclosures mentioned above be useful in improving audit quality and availability and delivery of audit services to public companies?*

Grant Thornton response: Audit firms operate in the public interest and are a critical component in the reliability of financial reporting, and we support requiring audit firms to provide certain governance disclosures to the extent that they provide stakeholders, particularly investors, with a better understanding of how audit firms and networks operate. Further, transparency of audit firm and network governance procedures, as well as additional information about quality control systems, could possibly enhance investor confidence in the overall sustainability of audit firms.

However, we do not believe that the proposed disclosures of audit firm governance would truly be useful in improving audit quality, and believe that audit firm transparency is not one of the primary drivers of confidence in financial reporting.

Instead, we believe that audit firm registration and independent inspections by audit oversight entities by reference to ISQC1 provide greater assurance of audit quality. Further, as discussed in the body of our response letter, the public disclosure of balanced inspection results for individual firms would provide further assurance to the public of an audit firm's quality.

Question 5: *Could other limitations arise if such disclosures were required?*

Grant Thornton response: We believe that the most significant limitation with respect to audit firm governance disclosures is that the link to audit quality has not been established. As noted above, however, we support disclosure of Article 40-type governance measures on the grounds that they may provide investors with a better understanding of how audit firms and networks operate and therefore could possibly enhance investor confidence.

Transparency of audit firms' audit quality indicators

Question 6: *Can audit quality indicators provide objective information when evaluating a firm's audit quality? If so, do the ones identified in this report accomplish that goal?*

Grant Thornton response: The input and output measures identified in section IV of the consultation paper could very well provide "objective" information in the sense that the measures could yield quantitative information about those specific items mentioned. We do not believe, however, that this information will provide "objective" information about a firm's audit quality, which we believe is an inherently qualitative determination. For example, the consultation paper states that "trends that indicate an audit firm has gained or lost a significant portion of audit business in a particular geographic region may provide an indication to the market about the quality of that firm's audit services in that area." We question whether such a trend necessarily provides an indication as to audit quality, for there are numerous other factors (e.g., pricing, marketing, etc.) that could explain the trend. In any case, we do not believe that it provides "objective" information about audit quality.

Auditing is an exercise that can be undertaken only by appropriately experienced practitioners, and we believe that some of the measures described in section IV of the consultation paper could be significantly misunderstood by investors and could be unfairly prejudicial to audit firms, if required to be disclosed to the public. We discuss the negative effects of public disclosure in more detail in our response to Question 17.

By contrast, audit oversight entities would likely be in a better position to assess the measures described in section IV of the paper, due to their expertise in the subject matter and their ability to view the information on a confidential basis and in the context of a thorough inspection of quality controls.

Question 7: *In addition to the indicators identified in this report, are there any other audit quality indicators that should be considered for disclosure? Would disclosure of the audit quality indicators described above be helpful in evaluating audit quality?*

Grant Thornton response: As noted in our response to question 6, we do not believe that public disclosures of the information set forth in section IV of the consultation paper will help the public evaluate audit quality. And, as noted in our response to question 17, some of the disclosures could be significantly misunderstood.

Question 8: *In addition to the benefits or limitations identified in this report, are there any other benefits or limitations about disclosing audit quality indicators that need to be considered?*

Grant Thornton response: As noted previously, we do not believe that there are benefits to the public of receiving the information described in section IV of the consultation paper. We also concur with many of the negative consequences set forth on pages 17-18 of the consultation paper. Please see our response to question 17 for further discussion of the limitations and negative effects of disclosure of the measures noted in section IV of the consultation paper.

Transparency of audit firms' financial statements

Question 9: *Can audited financial statements of audit firms provide useful or objective information regarding audit quality? If so, how?*

Grant Thornton response: Grant Thornton questions whether audited financial statements provide useful or objective information about audit quality or about the availability and delivery of audit services, and we are aware of no evidence suggesting that disclosure of financial statements will in fact improve audit quality. We therefore request that securities regulators give very serious consideration as to whether and how public disclosure of audited financial statements will positively impact audit quality.

Certain jurisdictions (the United Kingdom, for example) already require the public disclosure of audited financial information of those audit firms, which operate as Limited Liability Partnerships. All limited liability partnerships in the United Kingdom (not just audit firms) are required to publish audited financial statements. Thus, the disclosure requirements in the United Kingdom are not driven by audit quality concerns.

In addition, there are potential negatives associated with the public disclosure of audited financial statements:

- **Effect on liability.** We believe that regulators should consider the different liability regimes of various countries before making a global recommendation as to whether there should be public disclosure of audited financial statements. In some countries, the public disclosure of audited financial statements may have little effect on litigation against audit firms. In other countries, however, unwarranted litigation may increase if plaintiffs perceive audit firms as having “deep pockets” without regard to fault or the merits of their claims.

- **Effect on concentration.** We are also concerned with the effect that public disclosure of financial information could have on audit firm concentration. On the one hand, disclosure of audited financial statements might reveal that there are firms outside the big four that have the resources to audit large multi-national public companies, and might therefore contribute to easing concentration in the large public company audit market. On the other hand, however, audit committees might begin to choose firms with the greatest resources rather than those that offer the best fit, further cementing concentration. Further, smaller audit firms may believe that revealing full financial information would compromise a particular competitive advantage or undermine their partners' privacy. This may cause smaller firms to opt out of the public company audit market.

Question 10: *If disclosure to the public or regulators of an audit firm's own audited financial statements is warranted, who should audit the auditors? Are firms other than the Big Four equipped to audit the Big Four? If not, does having the Big Four firms audit each other raise concerns? If so, how could any such concerns be addressed?*

Grant Thornton response: If the disclosure of an audit firm's audited financial statements is required, firms other than the big four are unequivocally equipped to audit the big four audit firms. Indeed, in some jurisdictions non-big four firms do audit big four firms. For example, our Grant Thornton member firm in the United Kingdom audits Deloitte's UK member firm as well as KPMG Europe.

Grant Thornton is greatly concerned about audit firm concentration in the large public company audit market, and we believe that a very significant reason for such concentration is market misperception about the capabilities of audit firms outside the four largest firms. Many member firms of Grant Thornton are quite capable of auditing even the largest public companies in their markets, but our member firms are prevented from even competing for such audits in many cases by contractual limitations on choice of auditor. We believe that these contractual limitations stem from misperceptions about the capabilities of networks such as Grant Thornton, and we request that securities and audit regulators take steps to avoid inadvertently perpetuating these misperceptions. Indeed, it is unclear to us as to why IOSCO could believe this question was warranted.

We respectfully note that the consultation paper, via this question and in other places, perpetuates misperceptions that there are differences in quality and capability between the big four audit firms and other firms. For example, footnote 26 cites the UK transparency reports of only the big four firms, although Grant Thornton UK LLP and other firms also have public transparency reports. See <http://www.grant-thornton.co.uk/pdf/GT%20Transparency%20Report%2009.pdf>.

Question 11: *Can disclosing certain financial information instead of audited financial statements achieve the same objective of improving audit quality and the availability and delivery of audit services? If so, what financial information should be disclosed?*

Grant Thornton response: We do not believe that there is a correlation between the disclosure of financial information and the quality of audits that a firm provides or the ability of a firm to deliver audit services. These matters are best assessed by an in depth

knowledge of the firm and the firms' system of quality control. This knowledge is obtained by audit firm oversight bodies through an inspection process and is often communicated to the public through disclosure of inspection reports.

Parameters of enhanced disclosure for audit firms

Question 12: *Are there other parameters that should be considered?*

Grant Thornton response: Grant Thornton believes that the list of considerations set forth in section VI of the paper is comprehensive. The key consideration, of course, is whether disclosures will actually enhance an understanding of audit quality.

Question 13: *Should certain disclosures not be publicly available and if so, what criteria should be considered when determining what disclosures should be publicly available?*

Grant Thornton response: As noted above, Grant Thornton believes that the question of public versus private disclosures is critical. Certain disclosures should be made only confidentially to regulators and not to the public at large. We agree with the statements in the consultation paper that there are different constituencies in the financial reporting process, most notably, investors, regulators and audit committees, and each has a distinct role and distinct information needs.

In terms of criteria for determining which disclosures should be made public and which should remain private, we believe that the place to start is to consider the primary role and function of each stakeholder and to assess which stakeholder is best equipped to understand and appropriately make use of the particular disclosure. Significant consideration should also be given to the potential negative consequences of public disclosure, especially if the purposes of requiring the disclosure can be satisfied by providing such information privately to regulators.

To use one example, the consultation paper often references concerns about the availability and delivery of audit services and the desire to ensure the viability of audit firms. We believe that these considerations are the province of regulators, and further, that regulators are best able to understand these disclosures without the negative consequences of public disclosure. Therefore, disclosures of measures that are specifically related to these considerations, such as selected financial information and disciplinary proceedings, for example, should be provided only to regulators.

Question 14: *Should certain disclosures be made at the network, firm, and/or, engagement level?*

Grant Thornton response: The answer to this question generally depends on the nature of the information sought. We believe that in most cases, disclosure should be made at the firm/national level, because firms are independent legal entities, information is often available only on a firm-wide basis, and firms are regulated at a national level. In certain instances, however, some information might be consistent throughout a global audit network, such as network-wide quality control practices, and therefore network-wide disclosures may be appropriate. We believe that disclosure of engagement level information

would generally not be appropriate, other than to a regulator as part of an inspection or to audit committees.

Question 15: *Should there be different disclosure requirements for large, mid-size, and small audit firms?*

Grant Thornton response: We do not believe that there should be different disclosure requirements for large, mid-size, and small audit firms, although we recognise that different firm structures may require firms of different sizes to answer questions somewhat differently. Requiring different disclosures for different sized firms presents a risk that smaller audit firms would be discouraged from increasing their size in order to avoid the incremental costs associated with the additional disclosures that might be required of larger audit firms. Although this might present a commercial advantage to larger firms such as the member firms of Grant Thornton, we question whether such an outcome would be in the public interest because it has the potential to sustain concentration. If the Task Force considers requiring different disclosures, we suggest that it engage with smaller audit firms to determine how such requirements could act as an incentive and not a barrier to those who wish to enter the large corporate audit market.

Question 16: *Should the disclosures be mandatory and if so, should they be subject to regulatory oversight? Would a similar impact to the markets occur if the disclosures were encouraged instead of being mandatory? Should consideration be given to a framework of audit quality and allow for flexibility in the types of disclosures?*

Grant Thornton response: We believe that disclosures need not be mandatory because audit firms currently have significant incentives, including reputational, to disclose various governance measures publicly. As a practical matter, however, many of the disclosures referenced in the consultation paper are essentially required to be provided confidentially to regulators as part of the inspection process.

With respect to public disclosures, we believe that consideration should be given to establishing a broad framework with respect to audit quality. This would allow firms to consider which policies positively affect audit quality, and could provide a mechanism for firms to state how they seek to ensure audit quality. The operation of the free market ensures that if a firm believes it has a competitive advantage of disclosing information publicly, then it will do so. At present, firms disclose significant information publicly, but we have not heard that the public has been greatly interested in such disclosures.

Summary

Question 17: *Would transparency of audit firms improve audit quality and the availability and delivery of audit services? What negative effects, including costs, of increased transparency should regulators consider?*

Grant Thornton response: As noted above, Grant Thornton believes that the public disclosures required by Article 40 of the 8th Directive are appropriate. As mentioned above, we have already provided such disclosures at the network level to the extent they apply to an entity that does not provide audit services. Transparency is important for investor confidence in financial reporting, and regulators should assess how Article 40 disclosures affect audit quality before requiring public disclosures beyond those set forth in Article 40.

Potential negative effects that regulators should consider with respect to requiring disclosures beyond those set forth in Article 40 include:

- An increase in audit firm concentration, if disclosures make it more likely that shareholders and audit committees hire firms with the most resources instead of those firms that might be the best fit for the client, or if the requirement to provide disclosures causes some firms to not enter the public company audit market.
- Increased costs associated with additional disclosures.
- The possibility that certain disclosures (eg, workload, leverage, number of restatements) could potentially be misunderstood by investors.
- An increase in unwarranted litigation, if certain plaintiffs choose to file lawsuits on the basis of the financial resources of audit firms instead of on the merits.
- The fact that certain disclosures may not be indicative of audit quality. Requiring the disclosure of certain metrics could cause audit firms to manage their businesses to positively affect such metrics. If these metrics are appropriate factors in measuring audit quality, then this change in audit firm behaviour would be positive. If, however, these metrics do not measure or impact audit quality, then limited resources would be focused on matters unrelated to audit quality and perhaps away from matters that truly improve audit quality but which cannot be quantified.

Question 18: *Would investors have increased confidence in financial reporting as a result of increased audit firm transparency?*

Grant Thornton response: The types of public disclosures required by Article 40 of the 8th Directive may lead to increased confidence in financial reporting. However, Grant Thornton believes that there are better mechanisms to promote increased confidence in financial reporting. One such mechanism is audit oversight. Over the past decade, many of the developed countries around the world have developed audit oversight authorities. The presence of capable and independent audit oversight entities means that firms provide information about audit quality directly and on a confidential basis to audit regulators, who are in the best position and have the most expertise to assess audit quality.

Further, as discussed in more detail in the body of our letter, we believe that a rigorous inspection process is important to enhancing audit quality, and the public disclosure of fair and balanced inspection reports could enhance the public's knowledge about the audit firms and help drive audit quality. Moreover, we believe that balanced inspection reports may well help reduce concentration in the large public company audit market by addressing market misperceptions about the quality of smaller audit firms.

Question 19: *Are there significant benefits to investors of increased audit firm transparency, since they invest in companies and not audit firms?*

Grant Thornton response: Article 40 type disclosures may in fact increase confidence in financial reporting, although we believe that further study should be done to confirm this.

Further, as we note previously, different stakeholders have different roles to play in financial reporting, and the fact that investors invest in companies and not audit firms means that the types of disclosures they could receive should be more limited than those provided to regulators.

Question 20: *Should regulators consider areas outside of audit firms' governance, audit quality indicators, and financial statements for potential disclosures?*

Grant Thornton response: No. We believe that these areas are sufficient.



PP/BPC-SUB/mb

Mr Greg Tanzer
Secretary General
IOSCO General Secretariat
Calle Oquendo
28006 MADRID
Spain

Email: AuditorTransparency@iosco.org

15 January 2010

Dear Mr Tanzer

PUBLIC COMMENT ON THE TRANSPARENCY OF FIRMS THAT AUDIT PUBLIC COMPANIES: CONSULTATION REPORT

The Business Policy Committee is the Institute's committee which monitors developments in the rules and regulations affecting businesses generally and considers legislative and other proposals deriving from bodies such as HM Treasury, BIS, the FRC, the FSA, IOSCO and the European Commission. The Committee is broadly based, with members representing different sizes of accountancy practice, industry, the investment community, and the legal profession.

As the Institute's Charter requires, we act in the public interest, and our proactive projects, responses to consultation documents etc. are therefore intended to place the general public interest first, notwithstanding our charter requirements to represent and protect our members' interests.

The Committee's consideration of the above consultation report focused on the potential effects of enhanced transparency of audit firms, specifically whether it will improve audit quality and the availability and delivery of audit services.

The Committee acknowledges the global work that IOSCO undertakes in relation to accounting and finance related matters and is fully supportive of its efforts surrounding the issue of transparency of firms that audit public companies.

The Committee's views on the transparency of firms that audit public companies are set out below.

Audit Quality

The Committee discussed the merits of having a standard definition of audit quality and concluded that even if it such a definition could be agreed, there would be no absolute correlation between enhanced audit firm transparency and audit quality.

For the UK in particular, it could be argued that the Audit Inspection Unit (AIU) of the Professional Oversight Board (POB), part of the Financial Reporting Council (FRC), is the arbiter of audit quality.

The main aim in this type of regulation is to ensure there is public confidence in corporate reporting and governance: one way of achieving this is to make sure that the users of financial information are able to have confidence in, and place reliance on, the audit opinions of those businesses that are either listed on a recognised stock exchange or deemed to be a major public entity.

There are many factors that would need to be considered when forming this view such as the appropriateness of significant audit judgements exercised and the sufficiency of the audit evidence as well as other qualitative characteristics of the audit firm itself such as its leadership, strategy and communications. The policies and procedures on areas of audit methodologies, independence and ethics would also be examined.

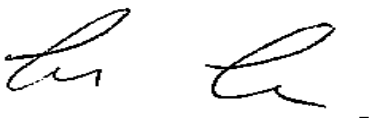
So whilst it is difficult to have a definitive “catch all” definition of audit quality (and it is not necessarily the case that this is ultimately needed), there are certainly characteristics of the qualitative information available which would indicate the existence of audit quality.

Transparency

The major audit firms in UK already make their transparency reports available online through their websites and there has been no compelling evidence presented to date which suggests that the availability of these reports has improved either audit quality or the availability or delivery of audit services.

We hope these comments have been useful to you and please do not hesitate to contact me if you want to discuss any of these points further.

Yours sincerely



PAUL PROVAN
Assistant Director, Business Policy
Secretary to Business Policy Committee



INSTITUTO DE
CENSORES JURADOS
DE CUENTAS DE ESPAÑA

Mr. Greg Tanzer
Secretary General
IOSCO
C/ Oquendo,12
28006 - MADRID
AuditorTransparency@iosco.org

Presidente

15 January 2009

Re: Consultation IOSCO: Transparency of Firms that Audit Public Companies

Dear Sir,

The ICJCE welcomes the opportunity that IOSCO is giving to the profession to comment on the Consultation on the transparency of firms that audit public companies. In general terms we are of the opinion that the 8th Company Law Directive that regulates the statutory audit in the UE and which is now in process of transposition into the Spanish Law, is designed to enhance and to harmonize the audit quality throughout all the European Union, and constitutes an appropriate legal framework for that purpose.

- The education requirements to access the profession
- The independence and ethical requirements to auditors
- The use of the International Standards on Auditing ISAs

are clearly addressing audit quality, furthermore, requirements on Transparency of audit firms auditing Public Interest Entities, addresses the auditors' Transparency.

As representatives to the Spanish Audit profession, grouping more than the 80 % of the turnover of the sector and near the 99% of the firms auditing listed companies, ICJCE contributes to promoting audit quality in Spain. ICJCE also contributes through an internal Quality Control system applicable over its members and in collaboration with the Spanish regulator, ICAC.

Please see our detailed answers to the questions below. Should you have any question or if you wish to comment personally the content of this letter, please do not hesitate to contact me at presidencia@icjce or our International Department Director at internacional@icjce.es we will be pleased to meet you at your convenience.

Yours sincerely

Rafael Cámara Rodríguez-Valenzuela



1. Is a definition of audit quality necessary to evaluate audit quality or can audit quality be evaluated from an understanding of the attributes, behaviors, and indicators of audit quality?

The 8th Company Law Directive is concerned about the consistent high quality of all the statutory audits. Auditors have to meet education, CPD, ethical and independence requirements and all audits should be carried out on the basis of the International Standards on Auditing, ISAs, but it does not include a definition of audit quality nor indicators to measure it.

Quality is assessed through quality assurance reviews within the firms and externally by the Oversight bodies. The Quality Assurance Systems assess the compliance with ethical and independence rules, with the technical standards and with the internal quality control of the firm.

Finally these procedures are checked through the review of audit files where the professional judgments of the auditor are also reviewed and contrasted. Professional judgment is an important part of the audit performance and cannot be measured by objective indicators.

Due to all the above mentioned, in general terms, we cannot see any advantage in creating a set of indicators to assess the quality of the work since we are of the opinion that it is impossible to establish a meaningful set of these indicators and could have, if the indicators are not disclosed together with other relevant information and in the appropriate context, the opposite effect as the information may be misunderstood.

2. In addition to competence and industry expertise of the audit personnel, firm culture that promotes audit quality, firm-wide quality control systems, and auditor oversight, are there other examples of attributes, behaviors, and indicators of audit quality that should be considered?

The audit quality indicators as described on pages 13 to 17 indeed provide information about the quality of an audit and they are finally assessed in a quality assurance review among other issues.

But as stated before we consider that a table of indicators cannot assess the quality of an audit and may lead the reader of the information to wrong conclusions. For example most of the indicators described in the report would need additional information to put them into the proper context and in some circumstances these disclosures could be related to a specific audit engagement.

3. Are there other areas of governance for which additional transparency should be considered?

The scope of article 40 of the Statutory Audit Directive and the IOSCO Consultation Paper is the same. The ICJCE believes that the information



provided in such transparency reports in accordance with article 40¹ of the Statutory Audit Directive provides a high level of transparency for audit firms auditing public interest entities

The EC Recommendation on Quality Assurance also requires some publicity of the results of quality assurance reviews and finally a link between the bad performance of an auditor with the start of an inspection or sanctioning procedure which results are also disclosed to the public.

Therefore we do not see the need of further disclosures other than those stated in the art 40 of the 8th Directive and in the EC Recommendation on Quality Assurance.

4. Would the proposed disclosures mentioned above be useful in improving audit quality and availability and delivery of audit services to public companies?

The ICJCE considers that audit quality enjoys a well deserved reputation although quality is something that always can be improved. We want to make reference to the IAASB project on that issue.

On the other hand, as stated in our answers to prior questions, the 8CLD is also dealing with audit quality but due to the short time since its implementation in the EU, the effects on audit quality and transparency are limited and difficult to assess. Therefore we are of the opinion that we should wait until a proper implementation of the Directive to assess its effectiveness in the improvement of audit quality and transparency before taking new actions at international level.

5. Could other limitations arise if such disclosures were required?

¹ Art 40 of the 8th Company Law Directive (Directive 2006/43/EC)

1. Member States shall ensure that statutory auditors and audit firms that carry out statutory audit(s) of public-interest entities publish on their websites, within three months of the end of each financial year, annual transparency reports that include at least the following:

- (a) a description of the legal structure and ownership;
- (b) where the audit firm belongs to a network, a description of the network and the legal and structural arrangements in the network;
- (c) a description of the governance structure of the audit firm; (d) a description of the internal quality control system of the audit firm and a statement by the administrative or management body on the effectiveness of its functioning;
- (e) an indication of when the last quality assurance review referred to in Article 29 took place;
- (f) a list of public-interest entities for which the audit firm has carried out statutory audits during the preceding financial year;
- (g) a statement concerning the audit firm's independence practices which also confirms that an internal review of independence compliance has been conducted;
- (h) a statement on the policy followed by the audit firm concerning the continuing education of statutory auditors referred to in Article 13;
- (i) financial information showing the importance of the audit firm, such as the total turnover divided into fees from the statutory audit of annual and consolidated accounts, and fees charged for other assurance services, tax advisory services and other non-audit services;
- (j) information concerning the basis for the partners' remuneration.



Reference is made to Art 40 in the 8CLD that allows not applying the provisions states in this article in special circumstances which could threat the personal security of a person. Disclosure of any information which publicity may threat personal or commercial privacy should be limited.

6. Can audit quality indicators provide objective information when evaluating a firm's audit quality. If so, do the ones identified in this report accomplish that goal?

As indicated above, the ICJCE is of the opinion that a table of indicators cannot asses the quality of an audit as it is impossible to establish a comprehensive set of objective and measurable indicators.

7. In addition to the indicators identified in this report, are there any other audit quality indicators that should be considered for disclosure? Would disclosure of the audit quality indicator described above be helpful in evaluating audit quality?

We refer to the comments in prior questions. With regard to particular disclosure proposals in the consultation we share the views of FEE as expressed in its letter of 15th of January regarding, insurance coverage, restatement and acceptance of clients.

8. In addition to the benefits or limitations identified in this report, are there any other benefits or limitations about disclosing audit quality indicators that need to be considered?

We do not have any further comment in this regard.

9. Can audited financial statements of audit firms provide useful or objective information regarding audit quality? If so, how?

The ICJCE is of the opinion that it is not the objective of an audit to give an opinion on the quality of the output or performance of a business, should it be an audit firm or a company in another industry or sector, but of its financial situation which is the result of different factors as for instance the quality of the output of the business.

Thus, there is no apparent link between the financial statements or financial information of audit firms and the quality of the audits carried out by the respective firm.

On the other hand this could harm competition among smaller and mid-sized audit firms, and could ultimately have an impact on the sustainability of the profession because it may encourage groundless claims to audit firms and increase the so called deep pocket syndrome.



10. If disclosure to the public or regulators of an audit firm's own audited financial statements is warranted, who should audit the auditors? Are firms other than the Big Four equipped to audit the Big Four? If not, does having the Big Four firms audit each other raise concerns? If so, how could any such concerns be addressed?

From the point of view of difficulty, the audit of the financial statements of a big firm does not differ from another audit in other sectors. In fact there are actual examples of Big Four practices audited by mid tier firms.

11. Can disclosing certain financial information instead of audited financial statements achieve the same objective of improving audit quality and the availability and delivery of audit services? If so, what financial information should be disclosed?

Following our answers to questions 3 and 9 above, in our view no additional requirements setting out new disclosures for audit firms should be introduced other than that required by article 40.

12. Are there other parameters that should be considered?

We refer to our answer to question 3.

13. Should certain disclosures not be publicly available and if so, what criteria should be considered when determining what disclosures should be publicly available?

As stated in our prior answers, the ICJCE is of the opinion that disclosures as stated in article 40 of the 8CLD are enough and mandatory for those audit firms auditing PIE despite of their size. The ICJCE agrees that different stakeholders have different needs and therefore there is some information which is extremely confidential and related to the business of a company, the audit firm or its clients, that should not be disclosed to the public but to the oversight authorities in the quality assurance reviews or to the audit committee of the concerned company.

Oversight bodies play a key role in protecting investors, have the expertise and are best positioned to evaluate information about audit firms. Investors rely on the information provided by the oversight bodies; therefore we do not see the need to disclose all the information to the general public. In this regard, the fact that some information only by used under confidential basis by the oversight body allows a more constructive flow and exchange of information, including the fact that there already exist legal restrictions related to confidentiality. We also refer to our answer to question 2.



14. Should certain disclosures be made at the network, firm, and/or, engagement level?

The level at which information should be disclosed depends on the type of information. As stated before the ICJCE considers that the information that should be disclosed in the transparency report is appropriate and no further disclosures are needed.

15. Should there be different disclosure requirements for large, mid-size, and small audit firms?

In line with our prior comments disclosure requirements as stated in Article 40 of the 8CLD are appropriate for audit firms auditing PIEs regardless the size of the auditing firm. This information may increase the confidence on the auditors' report and finally on the financial report. In the current times in which confidence in financial information is of the highest importance, the cost that firms will assume due to this new obligation are compensated by this increasing confidence.

Despite the size of the firm, additional transparency requirements should be avoided if there is no direct link with a greater level of quality, which in our opinion, is not the case. Specifically regarding the SMPs the cost of additional requirements would outweigh any benefit in transparency and finally may hamper the entrance of SMPs in the audit of listed companies' market.

16. Should the disclosures be mandatory and if so, should they be subject to regulatory oversight? Would a similar impact to the markets occur if the disclosures were encouraged instead of being mandatory? Should consideration be given to a framework of audit quality and allow for flexibility in the types of disclosures?

The ICJCE is of the opinion that disclosures as stated in Article 40 of the 8CLD should be mandatory for those audit firms auditing PIEs. No additional requirements should be stated and, should it be the case, they should be provided on a voluntary basis.

Furthermore having multiple disclosure requirements may suppose in addition to an increase of the cost and an important burden for the firm, a new risk due to the possible conflict with local confidentiality regulations. This is specifically important for audit firms providing audit services for multi-national companies. In this regard we ask for a consistent approach across jurisdictions based on Article 40 of the 8CLD that would enable investors and other stakeholders to better understand the information.

17. Would transparency of audit firms improve audit quality and the availability and delivery of audit services? What negative



effects, including costs, of increased transparency should regulators consider?

We refer to our answer to question 15 and 16.

18. Would investors have increased confidence in financial reporting as a result of increased audit firm transparency?

ICJCE believes that investors would have increased confidence as a result of increased transparency as stated in our prior answers.

19. Are there significant benefits to investors of increased audit firm transparency, since they invest in companies and not audit firms?

The ICJCE believes that investors would have benefits of increased firm transparency because of inherent benefits derived from transparency

20. Should regulators consider areas outside of audit firms' governance, audit quality indicators, and financial statements for potential disclosures?

As stated in our previous answers due to the close transposition of the 8th Company Law Directive² the ICJCE does not see a need to further regulate transparency)

² Text of the Bill to amend the Auditing Law (Act 19/88 of 12th July on Auditing):

«Article 14.b Annual Transparency Report (free translation of the text)

1. Individual auditors and audit firms auditing public interest entities and third countries audit firms are required to post on their websites an annual transparency report within three months after the financial year end, which shall include at least the following information:

- a) a description of the legal structure and ownership in case of an audit firm
- b) If the audit firm or the individual associated to those stated in article 8 ter c) and d) a description of the entities and individuals and also of the agreements or statutory relationships governing this association.
- c) a description of the governance structure of the audit firm.
- d) a description of the internal quality control system of the audit firm or individual and a statement by the administrative or management body on the effectiveness of its functioning including the date of the last Quality Assurance Review
- e) a list of public-interest entities for which the audit firm has carried out statutory audits during the preceding financial year;
- f) Information about the audit firm's or individual independence practices including a reference to the internal review of independence compliance has been conducted
- g) Information about the policy followed by the audit firm concerning the continuing education of statutory auditors
- h) financial information showing the total turnover divided into fees from the statutory audit of annual and consolidated accounts, and fees charged for other services,
- (j) information concerning the basis for the partners' remuneration

January 15, 2010

541/584

Mr Greg Tanzer
Secretary General
IOSCO General Secretariat
Calle Oquendo 12
28006 Madrid
Spain

By Email: AuditorTransparency@iosco.org

Institut der Wirtschaftsprüfer
in Deutschland e.V.

Wirtschaftsprüferhaus
Tersteegenstraße 14
40474 Düsseldorf
Postfach 32 05 80
40420 Düsseldorf

TELEFONZENTRALE:
+49 (0) 211 / 45 61 - 0

FAX GESCHÄFTSLEITUNG:
+49 (0) 211 / 454 10 97

INTERNET:
www.idw.de

E-MAIL:
info@idw.de

BANKVERBINDUNG:
Deutsche Bank AG Düsseldorf
BLZ 300 700 10
Kto.-Nr. 7480 213

Dear Mr Tanzer

Public Comment on the Transparency of Firms that Audit Public Companies: Consultation Report

The Institut der Wirtschaftsprüfer (IDW) [Institute of Public Auditors in Germany] is pleased to have the opportunity to comment on the above-mentioned consultation report. We fully agree with IOSCO's statement on page 1 of the consultation report that both audit quality and the availability and delivery of audit services is important to investors and other stakeholders. Not least because there have recently been diverse discussions around this and other related issues, we believe it is useful for IOSCO, in its role as an international body, to consider whether or not increasing the transparency of information about individual audit firms could realistically be expected to bring improvements to either, or indeed both, of these two aspects.

This letter includes certain comments of a general nature and also comments on specific matters, which we believe are significant in the context of the current debate on Transparency of Audit Firms that Audit Public Companies. Our responses to the questions posed in the consultation report are included in an Appendix to this letter.

GESCHÄFTSFÜHRENDER VORSTAND:
Prof. Dr. Klaus-Peter Naumann,
WP StB, Sprecher des Vorstands;
Dr. Klaus-Peter Feld, WP StB CPA;
Manfred Hamann, RA

page 2/12 to the comment letter to IOSCO dated January 15, 2010

General Comments

Need to Identify the Problem and Address the Issue in the Market as a Whole

The overarching problem IOSCO is seeking to address with its current initiative (in the consultation report on non-professional ownership structures and also, to a lesser extent, in certain considerations in the consultation report on auditor communications as well as this consultation report) appears to us not to be just concentration in the large public company audit market, experienced for some time now in many jurisdictions, per se, but also securing the ongoing ability of large public companies to acquire audit services that they and investors need, should one firm leave this market.

As we have also mentioned in our comment letter on the IOSCO Consultation Report on Exploration of Non-Professional Ownership Structure for Audit Firms, we believe that IOSCO has, in addressing these concerns, concentrated on only a few specific aspects, disregarding many other factors. Hence, there are many issues to be explored further, including but not limited to liability regimes in individual jurisdictions, the way in which audit committees operate etc., if current concentration is to be eased or the threat of a firm leaving the market decreased. There are very complex interactions in these issues. We have therefore found that it is not possible to provide a meaningful response to all questions posed in this consultation report in isolation.

Additional Disclosure as Inadequate Tool to Solve the Identified Problems

According to our understanding the basic theory behind the concept of increased transparency of certain factors (whether actually or only allegedly) pertaining to audit quality is that audit quality will be enhanced, resulting in stimulation of competition driven by audit quality. This, in turn, would be expected to ease concerns about the ongoing availability of audit services to large public companies because of a reduced risk of one or more of the existing large audit firms leaving the market and/or inducing smaller firms to enter this market segment. For several reasons we believe, however, that this concept is flawed, mainly because:

- We are not aware of any evidence to date suggesting a positive correlation between the disclosure to the general public of certain “quality drivers” and actual audit quality. Thus, we are concerned that such transparency as discussed in the consultation report might lead to considerable additional costs on part of the firms providing as well as those using the information without corresponding benefits

page 3/12 to the comment letter to IOSCO dated January 15, 2010

- Indeed, incentives to perform high quality audit work appear to be driven mainly by other factors, including the oversight systems to which audit firms are already subject and audit clients' demand for high quality audit services. We believe that such existing mechanisms do work well and, at least in Germany, already serve to ensure that audit firms perform high quality audits.
- Hence, information on audit quality and/or factors pertaining to audit quality, respectively, needs to be transparent to auditor oversight authorities and to audit clients, but not to the general public. Transparency to these "stakeholders", however, already exists. For example, auditor oversight authorities, by means of inspections and similar instruments, generally have access to all such information within an audit firm as is necessary to allow them to make a comprehensive evaluation of the quality of the firm's audit work. Similarly, audit clients who demand high quality audits usually require, prior to engaging a particular audit firm, some form of demonstration of the firm's ability to deliver audit services of the desired quality.
- In contrast to the case of transparency to auditor oversight authorities and audit clients mentioned above, disclosure to the general public along the lines discussed in the consultation report must take into account that such disclosure might be subject to "boiler plating" as we discuss in more detail below.

Therefore, we do not believe that enhancing transparency by adding disclosures, however detailed such disclosures might be, will be able to achieve the aim stated on page 1 of the consultation report, i.e., neither will enhanced transparency be able to maintain and improve audit quality nor improve the availability and delivery of audit services. Rather, in our view, the limitations of additional disclosures, which are considered in the consultation report (in particular on pages 17 to 19) more than outweigh the potential benefits. Furthermore, additional disclosures might turn out to be more onerous for smaller and medium-sized audit firms than for larger ones, thereby having detrimental effect on competition in the audit market.

page 4/12 to the comment letter to IOSCO dated January 15, 2010

Comments on Specific Matters

Need to Consider Merits of Current Transparency Disclosure Requirements and Cost Aspects of Changes

It follows from our comments above that we fully agree with IOSCO that, before potential action to be taken can be determined, there is a need to discuss and seek input on the possible limitation and also negative impact of enhanced transparency, and also further believe that long-term consideration is needed.

For example, in the EU the transparency reports required pursuant to Article 40 of the 8th EU Directive are relatively new. All concerned need time to gain experience and assess the benefits of these reports before new elements are added to their scope or the circle of firms required to publish such reports altered. Indeed, the comments made in the summary at the end of the consultation report, with which we agree, indicate that it is far from proven that there is a case to increase the detail in disclosure already required in the EU. In respect of jurisdictions that currently do not require such disclosure, there may be some merit in considering the European experiences in exploring whether the introduction of such disclosure would be appropriate.

Furthermore, particularly in the current economic climate, it is essential to be very cautious in establishing measures that would result in costs without proven benefits. Costs to the market as a whole would ensue if audit firms were to be required to set up the processes and systems to enable them to gather and present the suggested disclosures. Again, the effects of these incremental costs might vary between individual audit firms, depending on their size.

Lack of Consideration of Behavioral Impacts

In our view, possible dysfunctional effects on audit quality and choice of audit services resulting from firms' reactions to any additional transparency requirements is a fundamental aspect that is not, but should have been, discussed in the consultation report. Page 3 of the consultation report speaks of using additional transparency in the potential creation of "*an environment where audit firms would compete on, and thus raise, audit quality*". However, this ignores the likelihood that firms would tailor their behavior and disclosures thereon to "meet the metrics", in a similar manner as can be observed where entities strive to meet specific indicators of financial performance in financial statements by focusing activities that "help make the numbers" to the long-term detriment of the entity, etc. To illustrate this point; if one criterion used to "judge" firms were the number of hours of CPD per employee, it would be possible for firms to use

page 5/12 to the comment letter to IOSCO dated January 15, 2010

slack out of the so called busy season to increase training hours, without real considering the quality of that training. Such “competition” would not actually enhance audit quality to any marked degree, but might well “look good on paper”. Similarly, including details such as average hours worked per week could lead to hours worked being incompletely recorded, thus adversely affecting audit quality if resource budgeting were flawed as a result.

In any case, as the perceptions of readers are beyond firms’ control, they are likely to be cautious in making disclosures and this will ultimately lead to so called boiler plate, further diminishing the usefulness of disclosures.

Size Differential Between the Largest Firms and their Nearest Contenders

One key issue not discussed in the consultation report seems to be that the “magnitude” of the cleft between the smallest Big Four firm and the largest medium-sized firm is, in many jurisdictions, such that the “enhanced transparency solution” discussed may well be unlikely to actually be capable of easing, much less rectifying the situation. Whilst this is alluded to in the consultation report in terms of size and experience with public companies or particular industries, there are other factors which we believe are equally relevant to this discussion. For one, there may be reluctance on the part of firms to enter the public interest audit market for various reasons (i.e., their chosen niche is satisfactory; they perceive a regulatory deterrent; fee pressure means it will not be sufficiently profitable even if the firm has sufficient funds; lack of necessary litigation insurance, etc.). In addition, we have noticed a tendency for networks to become more widespread and increasingly geared towards cooperation rather than name-only relationships.

We would like to stress that in formulating our responses to certain questions posed in the consultation report we do not purport to provide investors’ perspectives, as the IDW represents its members who are German public auditors. However, we trust that our comments will be helpful to IOSCO in its further consideration of this issue.

Yours sincerely



Klaus-Peter Feld
Executive Director

page 6/12 to the comment letter to IOSCO dated January 15, 2010

APPENDIX

Responses to Questions Posed in the Consultation Report

1. *Is a definition of audit quality necessary to evaluate audit quality or can audit quality be evaluated from an understanding of the attributes, behaviors, and indicators of audit quality?*

Developing a workable definition of audit quality will be extremely challenging, if not impossible to achieve. We would like to point out that the IAASB plans to undertake a project on audit quality, and has scheduled a discussion of a project proposal at its meeting in June 2010. In our view, the IAASB is the most appropriate body to undertake such a project at an international level.

Given the global reach of the larger accounting firms that generally service larger public companies, measures need to be taken to address this issue both at global and national levels. In our view, the global adoption of e.g., ISAs and ISQC 1, would go a long way to harmonizing audit quality.

A further issue relevant to an evaluation of audit quality is, however, from whose perspective audit quality is to be assessed. Regulators and investors may have different perceptions of, and thus criteria for, such an evaluation. Their different perceptions may result in an expectation gap in relation to audits. In this context, we also refer to our response to question 8.

2. *In addition to competence and industry expertise of the audit personnel, firm culture that promotes audit quality, firm-wide quality control systems, and auditor oversight, are there other examples of attributes, behavior, and indicators of audit quality that should be considered?*

As noted above, we believe that audit quality is also significantly governed by standards and their implementation applicable to the auditing profession and the environment in which the profession operates. These cover auditing, quality control, educational and CPD, ethical standards, professional standards as well as requirements for the approval of statutory auditors, and external auditor oversight regimes.

page 7/12 to the comment letter to IOSCO dated January 15, 2010

Without a clear understanding of these factors, readers will not be in a position to interpret the information in transparency reports as to what it means in terms of audit quality.

We also believe that findings from the project to be undertaken by the IAASB mentioned above will be relevant to this issue and should be taken into account.

3. *Are there other areas of governance for which additional transparency should be considered?*

As noted by the PCAOB among others, academic research has not found conclusive evidence for an association between certain factors and audit quality nor have they found that simplistic indicators are true measures of audit quality. Thus there does not appear to be a valid case to support expansion of disclosures already required/ made voluntarily, certainly not to the extent suggested.

In our view disclosure under Article 40 of the 8th EU Directive is sufficient at the present time; whereas the suggested disclosure in the consultation report is overly detailed.

4. *Would the proposed disclosures mentioned above be useful in improving audit quality and availability and delivery of audit services to public companies?*

We do not believe that enhancing transparency by adding disclosures, however detailed such disclosures might be, will be able to achieve the aim on page 1 of the consultation report to “*maintain and improve audit quality and the availability and delivery of audit services*”. In our view, the limitations of additional disclosures discussed on page 12 of the consultation report and in our comments above are very real and need to be given serious consideration.

For example, as discussed in our comment above headed: “Lack of Consideration of Behavioral Impacts” we doubt that it is realistic to expect enhanced transparency to have any significant impact on the quality of audits performed by individual firms.

5. *Could other limitations arise if such disclosures were required?*

In our view the cost to firms, and ultimately to the markets as a whole, of complying with disclosure requirements is a major issue to be considered, but

page 8/12 to the comment letter to IOSCO dated January 15, 2010

which has not been thoroughly addressed in the consultation report. There needs to be a proven benefit attaching to each disclosure which justifies its cost. This issue should not be viewed as a means of satisfying the “wish lists” for information of individual parties.

Given the level of detail proposed, various limitations are likely to occur. Comparability is likely to be severely impaired, in particular as the scope and detail of descriptive narrative may differ widely, for example, in relation to HR policies as described on page 11. Competitive disadvantages are likely to become clearer, potentially exacerbating the “concentration” situation rather than improving it. For example, firm secrets could be exposed, or perceived deficiencies may become exaggerated.

Also the information needs of the various stakeholders are not uniform. Some suggested disclosures may not be truly useful, for example, much of the proposed information is not really helpful in auditor appointment decisions (e.g., balance of power issues, etc. – as the impact on individual audits likely not readily assessable). Generally, audit committees will request detailed information from possible candidates; it is unlikely that disclosures alone can replace this type of selection process.

Other suggested disclosures may be dangerous. The merits, if any, for audit quality, of disclosing “*liability and insurance arrangements*” of networks as suggested on page 10 of the consultation report are likely to be outweighed by disadvantages such as selecting auditors with deepest [perceived] pockets. Furthermore, this aspect may be exacerbated by the unavailability of adequate insurance cover (here we refer to discussions within the second panel “Quality of financial Statement Audits Debated at IOSCO Roundtable” held June 1, 2007).

If all the information discussed in the consultation report were disclosed publicly there would be a significant information overload.

6. *Can audit quality indicators provide objective information when evaluating a firm’s audit quality. If so, do the ones identified in this report accomplish that goal?*

We refer to our responses above. In addition, there is a danger that over time, users’ expectations may lead to certain benchmarks evolving for example, which could lead to misinterpretations, given that companies subject to audit are not directly comparable and thus neither are their audits. For example, information as to hours planned for an audit may appear generous, whilst not

page 9/12 to the comment letter to IOSCO dated January 15, 2010

being capable of reflecting the replacement of fewer hours of an expert with more hours of less qualified staff – which would not reflect the impact on audit quality. Also reliability issues arise as to information so provided (who audits the auditor) given the competition connotations. In Germany, for example, the information provided in transparency reports is subject to scrutiny by the auditor oversight authorities. To the extent that this is not the case elsewhere, it may need to be addressed.

7. *In addition to the indicators identified in this report, are there any other audit quality indicators that should be considered for disclosure? Would disclosure of the audit quality indicator described above be helpful in evaluating audit quality?*

This question presupposes that disclosure impacts on the quality of audit work performed. As noted in our letter above, we do not believe this to be the case. We also refer to our response to question 1, in conjunction with our comment letter concerning the consultation report on auditor communications. Disclosure of the standards to which the firm adheres would only make sense when readers have a reasonable understanding of those standards and of the regulatory environment in which the firm operates.

8. *In addition to the benefits or limitations identified in this report, are there any other benefits or limitations about disclosing audit quality indicators that need to be considered?*

We refer to our responses above.

Being able to gauge audit quality from information made freely available depends on from whose perspective audit quality is viewed – shareholders/ those charged with governance/ management of the entity. As noted above in our response to question 1, these parties' perceptions of and desires for audit quality will differ depending on the perceived role of the audit – shareholder protection; support for non-executive directors or audit committee in their oversight role; etc.

page 10/12 to the comment letter to IOSCO dated January 15, 2010

9. *Can audited financial statements of audit firms provide useful or objective information regarding audit quality? If so, how?*

We would caution that any expectation that financial statements of individual firms might provide information sufficient to draw conclusions as to the quality of audit work undertaken by the firm is dangerous, because this financial information will necessarily be subject to interpretation. For example, profitability could actually result from a) high profit achieved for providing high quality audits, or b) high profit achieved because costs are cut at the expense of audit quality.

In Germany financial statements of major audit firms are published and have been for some considerable time. There is no evidence to suggest that this publication in itself has been a contributory factor in audit quality.

10. *If disclosure to the public or regulators of an audit firm's own audited financial statements is warranted, who should audit the auditors? Are firms other than the Big Four equipped to audit the Big Four? If not, does having the Big Four firms audit each other raise concerns?*

If so, how could any such concerns be addressed?

We refer to our response to Q. 9 above.

In our opinion, firms other than the Big 4 are able to audit the Big 4. This is the case in Germany.

11. *Can disclosing certain financial information instead of audited financial statements achieve the same objective of improving audit quality and the availability and delivery of audit services? If so, what financial information should be disclosed?*

We refer to our response to Q. 9 above.

12. *Are there other parameters that should be considered?*

As mentioned above, we believe the overall cost: benefit to the markets as a whole of adding any such measures is a key issue.

Many factors considered are already governed by either auditing standards, quality control standards and ethical requirements and the adherence thereto by individual firms is then also monitored both internally and externally. Thus, inessential repetition should be avoided otherwise unnecessary costs will occur

page 11/12 to the comment letter to IOSCO dated January 15, 2010

and be multiple. Disclosures in this context need to be a minimum and focus on only firm-specifics. Thus we also believe that educating interested parties as to these aspects is also a key issue that ought to be addressed. In this context we refer to comments in our letter on the consultation report on Auditor Communications.

13. Should certain disclosures not be publicly available and if so, what criteria should be considered when determining what disclosures should be publicly available?

As mentioned above, we believe the overall cost: benefit to the markets as a whole of adding any such measures is a key issue.

The general public at large will not have the requisite knowledge or ability to benefit – therefore a minimum of disclosures should be made public. Other matters should be disclosed to those who would need that particular information; this needs to be determined on a case-by-case basis.

14. Should certain disclosures be made at the network, firm, and/or, engagement level?

At which level disclosures would be appropriate is an issue that would seem to us need to be addressed on a case-by-case basis. For example, to the extent that particular quality control measures were at network level, it would make sense to address these at network level.

15. Should there be different disclosure requirements for large, mid-size, and small audit firms?

It would not be appropriate to require all audit firms to disclose the same information, for example, where different regulation or oversight applies this could be determined according to the needs of individual regulators.

As one problem that IOSCO is seeking to address is the effects of concentration in the large public company audit market, there would need to be sufficient disclosure to allow audit committees and others involved in auditor engagement to gain meaningful information about firms willing to enter that market; not only those already within that market.

page 12/12 to the comment letter to IOSCO dated January 15, 2010

16. Should the disclosures be mandatory and if so, should they be subject to regulatory oversight? Would a similar impact to the markets occur if the disclosures were encouraged instead of being mandatory? Should consideration be given to a framework of audit quality and allow for flexibility in the types of disclosures?

We refer to our general comments above.

17. Would transparency of audit firms improve audit quality and the availability and delivery of audit services? What negative effects, including costs, of increased transparency should regulators consider?

We do not believe transparency of audit firms would improve audit quality and the availability and delivery of audit services. We refer to our general comments above.

18. Would investors have increased confidence in financial reporting as a result of increased audit firm transparency?

We are not aware of any well founded basis to suggest this would be the case.

19. Are there significant benefits to investors of increased audit firm transparency, since they invest in companies and not audit firms?

We are not aware of any well founded basis to suggest there would be significant benefits to investors.

20. Should regulators consider areas outside of audit firms' governance, audit quality indicators, and financial statements for potential disclosures?

No. We refer to our comments above.

However, as also explained in our comments above, we do believe there are other regulatory aspects including auditor liability and possibly overly stringent independence requirements that regulators need to explore as an integral part of addressing concerns surrounding market concentration.



International Federation of Accountants

545 Fifth Avenue, 14th Floor, New York, NY 10017 USA
Tel +1 (212) 286-9344 Fax +1 (212) 286-9570 www.ifac.org

January 25, 2010

Mr. Greg Tanzer
Secretary General
IOSCO General Secretariat
Calle Oquendo 12
28006 Madrid
Spain
AuditOwnership@iosco.org

Re: Public Comment on the Transparency of Firms that Audit Public Companies: Consultation Report

Dear Mr. Tanzer,

The International Federation of Accountants (IFAC) values the opportunity to provide comment on the IOSCO paper, *Transparency of Firms that Audit Public Companies: Consultation Report*.

Attached is a submission that outlines the views of IFAC with respect to the central ideas discussed in the IOSCO paper. In developing our response, IFAC conducted some limited consultation with a number of our member bodies and members of the Forum of Firms.

In general, while we consider that transparency of audit firms is an important issue, and therefore support IOSCO's initiative in this area, we do not consider that further mandatory transparency requirements will impact significantly on either audit quality or the availability and delivery of audit services to public companies. We do identify the need for research, drawing on the use currently made of transparency information emerging from the reporting of oversight bodies and other empirical data, to assess whether stakeholders use this information in circumstances where audit quality is an important element in decision-making.

However, notwithstanding the general conclusion referred to in the paragraph above, IFAC considers that transparency is desirable for a number of reasons, including as evidence of sound corporate governance processes in organizations in which there is a significant public interest, and for these reasons we strongly support the codification and international alignment of transparency requirements.

Given the position taken in this submission we have felt it more helpful to organize our submission by reference to certain key issues, rather than by addressing the specific questions raised in consultation report. We hope that the views expressed in this submission assist IOSCO in the further development of its position on this matter.

If IOSCO seeks additional clarification or further consultation regarding the enclosed submission, please do not hesitate to contact me.

Sincerely,

A handwritten signature in black ink, appearing to read 'Ian Ball'.

Ian Ball,
Chief Executive Officer

The following document reflects the views of the International Federation of Accountants (IFAC). IFAC is the global organization for the accountancy profession. It works with its 159 members and associates in 124 countries and jurisdictions to protect the public interest by encouraging high quality practices by the world's accountants.

Introduction:

In its consultation report IOSCO has raised the issue of audit firm transparency as a mechanism to improve audit quality, and therefore the reliability of public company financial statements, and also to improve the availability and delivery of audit services to public companies.

IFAC considers audit quality to be critical to the functioning of capital markets. In examining the role of transparency of audit firms, it is necessary to consider the potential impact of additional transparency requirements in the context of the range of measures which are directed at the goal of achieving audit quality. The central question we will address is whether additional transparency will contribute significantly to further enhancing audit quality.

Similarly, in relation to the availability and delivery of audit services to public companies, the issue is whether additional audit firm transparency would likely have a significant impact on competition and choice in the market for audit services, given other characteristics of that market.

The submission below addresses these central questions, and concludes that additional transparency is unlikely to contribute materially to either of the stated goals.

The submission then addresses the reasons why a certain level of audit firm transparency is desirable, and proposes that the focus of international regulatory efforts be on identifying appropriate transparency around audit firm corporate governance and on achieving great international consistency in transparency requirements.

- 1. IFAC believes that increased audit firm transparency requirements will not be instrumental in achieving materially improved audit quality because existing regulatory, self-regulatory and market mechanisms create sufficient incentives for audit providers to conduct high-quality audits.**
 - a. Three categories of mechanism currently create a collectively significant range of incentives for audit service providers to ensure the quality of audits: *regulatory, self-regulatory and market mechanisms:*

Regulatory Mechanisms – Historically there has been a range of regulatory mechanisms employed to promote high-quality audits. In many jurisdictions, regulatory authorities have prescribed educational requirements, have registered audit practitioners and have prescribed restrictions on the ownership arrangements for audit firms, for example. Over the past decade this range of mechanisms has been substantially strengthened in numerous jurisdictions. These changes include, most significantly, the Sarbanes-Oxley Act in the United States and the subsequent establishment of independent audit oversight bodies in many other jurisdictions. Taken together, this range of regulatory mechanisms is designed to provide assurance to capital market participants that they can have confidence in the quality of audits. The recent developments in audit oversight have been very directly designed to address concerns over audit quality by giving the audit oversight bodies in most major capital market jurisdictions considerable and detailed access to the full range of information needed to form views not only on the firm level policies and structures but also on the actual conduct of specific audits.

Self-regulatory Mechanisms- The self-regulatory mechanisms administered by professional accountancy institutes prior to the regulatory changes referred to above still exist today, though in a modified form in many countries. These include such mechanisms as educational requirements and certifications mandated by professional accountancy institutes; requirements for continuing professional development; ethical codes which place requirements on auditors on matters such as auditor independence; auditing standards; and the organizational structures of firms and their ownership arrangements. It should be noted, however, that internationally there has been a trend for self-regulatory mechanisms to become externally regulated.

Market Mechanisms – Market mechanisms relate to the competitive incentives that exist for the provision of high quality audits, irrespective of the incentives around compliance with regulatory or self-regulatory requirements. These incentives derive ultimately from the value of an audit in lowering the cost of capital of the reporting entity. Any reduction in the cost of capital is contingent on the audit providing assurance on the reliability of the information reported to capital markets. Such assurance is in turn derived from the quality of the audit, a function of many elements, but especially the expertise and independence of the auditor. Market pressures should therefore provide incentives for transparency if additional disclosures about firm structures and processes provided convincing evidence of audit quality. Market mechanisms also create incentives to improve audit processes, whether to enhance the level of assurance or to provide the same level more efficiently. Additionally, markets provide incentives to mitigate the risks associated with poor quality audits, given the costs of contesting and settling litigation where poor quality audits are alleged.

When considering the potential benefit to be gained from mandating additional levels of audit firm transparency, IFAC's view is that it is highly unlikely that such additional transparency would have a significant, arguably even noticeable, effect on audit quality. We consider that, taken together, the three types of mechanisms above create considerable pressure to undertake high quality audits.

- b. A secondary point relates to the relative novelty of many of the regulatory changes of the past decade. Many of the changes are still recent, and to reach conclusions regarding their limitations or to the need for additional requirements such as further transparency seems premature. Similarly, some of the other factors which contribute to audit quality have also undergone significant, recent change. An example is the clarified set of International Standards on Auditing (ISAs), which are currently being implemented. Given the extent of recent change in areas which can be seen to have a very direct and significant impact on audit quality, our view is that further change in areas which impact less directly on audit quality should not be pursued at the present time.

While recognizing the risk to investors associated with placing excessive confidence in the audit inspection activities conducted in many jurisdictions, we nevertheless consider that the incentives around this mechanism in particular are significantly more powerful and more direct than those created by additional transparency. As the primary regulatory mechanism aimed at achieving audit quality, oversight bodies have access to information concerning firm structures and processes as well as very specific and detailed information related to the conduct of individual audits. Additionally, oversight authorities employ the professional expertise necessary to interpret and analyze significant quantities of information, and to form judgments on audit quality based on that information. Because of the specialized knowledge and institutional authority they possess, audit oversight bodies are uniquely placed to ensure that audit firms comply with the professional standards, legal requirements and regulatory provisions of their respective jurisdictions. Given that shareholders, investors and the general public would not, under any conceivable transparency regime, have access to the same breadth and depth of information, and nor would they have the same access to professional expertise, our conclusion is that, from a comparative perspective, additional transparency requirements are very unlikely to generate enhanced audit quality.

The analysis in the preceding paragraph reflects our informed opinion, given current knowledge. We are conscious, however, that conclusions on the role of transparency in assessing audit quality could be informed by empirical research. Audit oversight bodies, in at least some jurisdictions, report on many of the features of audit firms that the consultation report identifies as candidates for transparency reporting. Additionally, information may be available through reporting on peer

reviews of audit firms. To the extent that such reporting is sought and utilized in, for example, engagement decision-making by audit committees, it would seem possible to obtain empirical evidence bearing on the role of such information in decision-making where audit quality is important. Such research would, we believe, contribute to a better understanding of the role of transparency and we would welcome the opportunity to participate in the design and conduct of such research.

2. IFAC considers that increased measures of transparency would not enhance in any significant way the availability and delivery of audit services to public companies.

- a. IFAC considers that increased transparency requirements will do little to facilitate greater availability and delivery of audit services to public companies. There are a number of factors which have lead to the current level of concentration in the audit market and a range of actions which have been advocated as a means of mitigating that level of concentration. IFAC's view is that, while there is no single action which would address the current situation, and certainly not in a short time frame, there are a number of areas where action has the potential to be more effective than through increased transparency. Included amongst these is reform in the area of professional liability, which would not only reduce the risk of entering or expanding in the large public company audit market, but would also reduce the risk of losing one of the existing players in that market. We strongly support efforts to reduce barriers to entry to this market, where the elimination of those barriers will not compromise audit quality (see b. below). This is not to argue that the additional measures of transparency posed by IOSCO would have no bearing on marketplace dynamics and competition; however, we do not believe a strong enough case can be made to demonstrate that it would achieve an impact of any real significance, relative to other possible actions.
- b. There are a number of barriers to entry in the market for large public company audit services which restrict availability of audit services and contribute to the current state of audit firm concentration. These barriers, which are listed below, should be the subject of further research and debate. Key amongst them are the following:
 - i. International Regulatory Barriers - The complexity and diversity of regulatory regimes around the world present major barriers to entry into the global audit firm marketplace, by increasing the costs associated with this activity. Better regulatory coordination in respect to registration, licensing, inspection and other procedures that generate costs for global audit service provision could potentially reduce significantly both the level of investment and the ongoing operating costs necessary to engage in this market. The current

environment requires, for example, resources for staff coverage (experts who understand the local rules, laws and procedures) in different localities throughout the world. The greater the diversity of practice, the greater the investment in staff required to command, and remain current, across divergent regulatory regimes, including professional standards.

- ii. Professional Liability Risk - Professional liability presents a significant barrier to market entry. Without liability caps, proportionate liability, and/or other measures designed to protect firms from unlimited damages, the incentives to seek to expand in this area of activity (large, transnational public company audits) is reduced. As noted above, action in this area should also assist in reducing the risk of one of the existing large firms from exiting the market. IFAC's view is that, in the current state of the market, it is more important to focus on preventing any market participants from exiting the market than to look to enlarge the pool of audit firms. Although any unnecessary barrier to entry should be removed, enabling market entry and growth by the smaller of the current participants, the greatest risk to the market is the exit of a major current participant. This view is partly a reflection of the current structure of the market (referring to the gap between the Big 4 and other large global firms) and of the time needed to change that structure in any significant way.
- iii. Market Perceptions – One of the barriers to entry, or to enlargement of mid-tier audit firms, lies in market and possibly regulatory perceptions of the capacity of audit firms other than the “Big 4” to provide services of the required quality. For mid-tier audit firms to grow, it is critical that they have access to work for which they have the necessary capacity, and are not precluded from consideration for such assignments. While IFAC is of the view that perceptual barriers of this kind exist, this is a subject that requires further study and consideration, both as to the extent and seriousness of the problem and the possible avenues for addressing the issue.

A final comment in relation to the suggested disclosures in the consultation report is that, if there were a move to increased transparency requirements in the large public company audit market, it would be critical to take full account of the manner in which such changes might apply to smaller audit firms – in particular it would be important to ensure that the requirements did not flow through into the small practice sector in a manner which resulted in disproportionate costs, and therefore create or increase barriers to entry.

- 3. IFAC considers that all significant entities in which there is a public interest – which includes the auditors of public interest entities - should be subject to transparency requirements, especially in relation to their corporate governance arrangements. This issue requires more attention, but not primarily in relation to the two goals identified in the consultation report.**

IFAC's view is that there is a public interest in certain aspects of the operations of audit firms, given the importance of their role in providing assurance in a capital market context, and for this reason some level of transparency is required. Currently, such requirements vary markedly across different jurisdictions and the rationale for such requirements also varies markedly. In some cases the required transparency is associated with the legal form of the audit firm, in other cases the requirements relate more directly to the audit function and its role within the financial system. IFAC acknowledges that transparency requirements associated with the legal form of the organization are best considered within the context of the national or jurisdictional legal system. However, to the extent that transparency requirements derive from the public interest nature of the audit function, our view is that there should be greater international consistency in those requirements. While our view is that there needs to be further research in this area, we consider that the transparency requirements associated with the public interest role of audit are most likely to relate to issues of corporate governance, such as information concerning management structures, independent non-executives, compliance systems and similar aspects which provide shareholders of listed companies and other stakeholders (e.g., clients, creditors, and others in the financial community) with some indication of the quality of corporate governance.

- a. As noted in the consultation report, transparency requirements, similar in general terms to those discussed in IOSCO's paper, exist in a number of jurisdictions. The European Union's Article 40 of the 8th Company Directive is an example of one such system that has international application. Article 40 already requests comparable information to that proposed in IOSCO's paper (e.g., corporate governance structures, educational competencies, quality control systems, and the basis for remuneration). Given the relative novelty of these requirements, and the fact that they are applicable across a number of different countries with different legal systems and institutional arrangements, we would favor research into the impact of these disclosures as input to further consideration of this issue.
- b. Finally, IFAC is of the view that transparency requirements derived from the public interest role of auditing should, to the extent possible, be developed and applied in a consistent manner internationally, and presumably this is implicit in IOSCO addressing this issue rather than leaving it to be resolved in individual jurisdictions. Based on analysis and research into the set of

information which will assist investors and other external stakeholders to understand the quality of corporate governance in audit firms, our view is that the focus of the regulatory community should be on achieving consistency in transparency requirements.



International Headquarters
KPMG International
KPMG Building
Burg.Rijnderslaan 20
1185 MC Amstelveen
The Netherlands
Telephone 31 (20) 656 6858
Fax +31 (20) 656 6777

Correspondence Address
KPMG AG
Klingelhöferstraße 18
Vorstand
Berlin/W 10785
Germany
Telephone +49 30 2068-1480
Fax +49 1802 11991-1480

Greg Tanzer
Secretary General
IOSCO General Secretariat
Calle Oquendo 12
28006 Madrid
Spain

Our ref ws/dlg/181

15 January 2010

Dear Mr Tanzer

IOSCO Consultation on Transparency of Firms that Audit Public Companies

KPMG International Cooperative¹ (KPMG International) is pleased to respond to IOSCO's consultation on the Transparency of Firms that Audit Public Companies: Consultation Report issued in September 2009 (the "Transparency Consultation"). This response is submitted on behalf of the international network of KPMG member firms.

KPMG Supports Transparency

High quality audits of public companies are important to investor confidence in financial reporting and the strength and stability of the global capital markets. KPMG International has been a long-standing supporter of transparency reporting that enhances stakeholder understanding of the audit and of the measures that the firms take to enhance audit quality. In Sustaining Confidence in Global Capital Markets (2007)² we said that *"audit firms should operate in the public interest and Audit Committees (ACs), management, regulators, Governments and the public deserve a clear articulation of the steps audit firms are taking to uphold their professional obligations and responsibilities to the investing public, capital markets and clients."*

KPMG has evidenced this commitment to public transparency by publishing transparency reports at the KPMG International level and many KPMG member firms also publish transparency reports. We were the first global network to publish a Transparency Report (2005) and, in October 2009, we

¹ KPMG is a global network of professional services firms providing Audit, Tax and Advisory services to a wide variety of public and private sector organisations. KPMG International is a Swiss cooperative, a legal entity formed under Swiss law, with which all the member firms of the KPMG network are affiliated. KPMG International does not provide professional services to clients; audits of public companies together with other services are all provided by member firms.

² Sustaining Confidence in Global Capital Markets, KPMG International; January 2007. (p19)

updated our transparency report for KPMG International³ to align broadly with the requirements in Article 40 of the EU Statutory Audit Directive (“Article 40”).

We believe that audit firm governance has a significant influence on audit quality and an audit firm’s sustainability. Therefore, we support public disclosures regarding policies and structures that comprise how the entity is organized as well as the systems, controls, and procedures established to achieve audit quality. We believe that insight into our commitment to audit quality and the way we govern ourselves promotes public confidence in audit quality, which in turn promotes confidence in financial reporting and contributes to stable capital markets.

As the Transparency Consultation points out, many of the Article 40 disclosures relate to audit firm governance, including the organizational structure of the firm and its relationship to its network. Many KPMG member firms have been producing public transparency reports for several years and those within the European Economic Area (together with those non-EEA KPMG member firms auditing entities listed on EU regulated markets who have to register with an EU audit regulator) have or are in the process of publishing public transparency reports to conform with the requirements of Article 40. Thus, Article 40 could provide a global benchmark for public transparency disclosures and indeed is being considered as a framework on which to base transparency disclosures in other jurisdictions.⁴

Using Article 40 as the framework on which to base public transparency disclosures would have the added benefit of introducing global consistency in transparency and disclosure standards. Convergence to a globally agreed framework for public transparency disclosures will increase consistency and comparability, which will increase the usefulness of such reports to regulators, investors and those such as audit committees responsible for auditor selection while also allowing both regulators and regulated entities to focus once on the substance of such regulatory and reporting requirements rather than managing multiple overlapping but inconsistent reporting regimes. Further, we note that implementing consistent, globally agreed regulatory requirements is one of the objectives identified by the G20 leaders in their responses to the global financial crisis.⁵ To avoid increased cost and unnecessary duplication, and to minimize stakeholder confusion, jurisdictions should recognize transparency requirements that are equivalent and should not require additional or different disclosures.⁶

We believe that efforts to agree global standards for transparency disclosures should focus on public transparency disclosures. We believe that the disclosures considered by IOSCO that are supplemental

³ <http://www.kpmg.com/Global/en/WhoWeAre/Documents/Transparency-Report.pdf>

⁴ See, e.g., the final report of the U.S. Treasury Advisory Committee on the Auditing Profession recommendation 7 (p88), which “[u]rge[s] the PCAOB to require that, beginning in 2010, larger auditing firms produce a public annual report incorporating (1) information required by the EU’s Eighth Directive Article 40 Transparency Report as deemed appropriate by the PCAOB....”

⁵ London G20 Summit Communique, 2 April 2009 <http://www.londonsummit.gov.uk/en/summit-aims/summit-communique> para.14 “But we also agree to establish the much greater consistency and systematic cooperation between countries, and the framework of internationally agreed high standards, that a global financial system requires.”

⁶ For example, the Japanese Financial Supervisory Agency (FSA) accepts Transparency Reports issued by EU-based audit firms in accordance with Article 40 as complying with the FSA’s requirement that audit firms registered in Japan describe their status of quality control management, management structure and description of services rendered by the firm.

to those required by Article 40 are not suitable for universal public transparency disclosures due to legal or regulatory barriers that exist in some jurisdictions; see our comments under “Principles for Transparency Disclosures.” Additional information that is provided to satisfy requests from audit regulators should be agreed at a national level and subject to appropriate confidentiality protection.

KPMG Member Firms Are Transparent to their Audit Oversight Authorities and this Contributes to Audit Quality

Since IOSCO commenced its work on audit firm transparency, there has been a step change in the regulation of audit work and audit firms. Most developed economies, and many emerging economies, have established independent audit oversight authorities which have systems of registration, inspection and reporting that often includes requiring a wide range of disclosures by audit firms. Independent audit oversight authorities look carefully at the work of audit firms and their systems of quality control. We support this oversight and believe that these initiatives have been, and continue to be, important contributions to enhancing both audit quality and public confidence in audited financial reports. High quality audits preserve and enhance public confidence in financial reporting.

Transparency of audit firms with their oversight authorities plays a significant role in effective oversight of the profession, but the determination of what disclosures should be provided on a non-public basis to a firm’s regulators involve some different considerations from that of what disclosures should be provided to the public. Audit firms provide significant information to their home country regulators and in many cases also to foreign regulators with which they are registered. Much of this information is subject to confidentiality and other protections afforded by applicable laws and regulations. These protections serve to facilitate the supervisory dialogue, thus enhancing the ability of oversight authorities to engage in effective and robust oversight of the profession.

A number of audit regulators, some of whom are IOSCO members, have established the International Forum of Independent Audit Regulators (IFIAR) which now has 34 members. Representatives of IOSCO participate in IFIAR meetings as observers along with the Basel Committee on Banking Supervision, the Public Interest Oversight Board, the World Bank and the European Commission. As IOSCO knows, KPMG, together with the other large accountancy networks, have been involved in a constructive dialogue with IFIAR on a number of audit issues, including transparency and global consistency. One of IFIAR’s four main work streams is identifying drivers of audit quality.

We believe that any further work in the area of transparency and audit quality measures should draw together all regulators that have an interest in these issues and we think that IFIAR may be well placed to take a leading role. We also suggest that any further work be structured in such a way that it involves all stakeholders including not only audit firms but also investors and those responsible for auditor appointments. We believe that this is necessary in order to develop requirements that are responsive to the information needs of relevant stakeholders while recognising the wide range of legal and economic environments in which any globally agreed requirements would be applied.

Principles for Transparency Disclosures

We believe that when considering transparency disclosures audit firms might make in addition to disclosures about their governance and systems and processes for ensuring audit quality, the disclosure in question should be subject to a two-part analysis: (1) whether the disclosure is relevant to audit quality; and (2) whether the disclosure is understandable by stakeholders. Disclosures that do not meet these criteria should not be required to be made public. Our initial experience with the transparency disclosures required by Article 40 at both a network and member firm level generally has been that such disclosures meet these criteria. Disclosures that we believe do not meet these criteria and which were proposed in the Transparency Consultation includes voting rights, insurance and liability arrangements and audited financial statements.

Voting rights

We believe that a narrow focus on voting rights would fail to achieve the more important objective of describing a network's structure and providing an overview of its governance arrangements. See, for example, our description of the structure and governance arrangements for the KPMG network in our 2009 Transparency Report.⁷

Insurance and liability arrangements

We do not support introducing requirements to disclose insurance and liability arrangements within a network. Such information is of considerable commercial sensitivity, which has been recognised by governments and regulators, as noted in the London Economics report on auditor liability that was prepared for the European Commission.⁸

Financial statement disclosure

There are jurisdictions where KPMG member firms are required to provide financial statements, for example as a consequence of electing a limited liability form of organisation within the EU. However, for other member firms such disclosures may not be appropriate due to the legal environment in which they operate. We believe that requirements regarding financial information should be developed at a national level to reflect the legal environment, and, in particular the liability exposure, of a particular country. We believe that a universal requirement for financial statements could pose threats to the sustainability of firms in some countries thereby reducing rather than expanding choice.

We agree that audit firm sustainability is a legitimate concern for both audit committees and capital market regulators. However, audit firm sustainability is an area that we believe should be addressed confidentially. Further, we believe that focusing on financial statements as a measure of sustainability is an overly narrow approach. One of the lessons from the collapse of the Andersen network is that it

⁷ KPMG International Transparency Report, October 2009

<http://www.kpmg.com/Global/en/WhoWeAre/Documents/Transparency-Report.pdf> (p4-10)

⁸ Study on the Economic Impact of Auditors' Liability Regimes (MARKT/2005/24/F) by London Economics
http://ec.europa.eu/internal_market/auditing/docs/liability/auditors-final-report_en.pdf, part II.

is public confidence, not available capital, that can be critical to a firm – and network’s – survival. We continue to believe that, in order to address audit firm sustainability, what is needed is measured liability reform that protects audit firms from catastrophic claims but not from wilful misconduct or gross negligence.⁹ We believe that the EU study and liability recommendations¹⁰ may be a good starting point. Therefore we do not support a universal requirement to provide financial statements to the public for the aforementioned reasons and we are not aware of any evidence, nor do we consider it likely, that the publication of financial statements contributes in any way to audit quality or competition.¹¹

Audit Quality Indicators

We believe that there is no agreed consensus at this time regarding audit quality indicators. Although there has been some debate around this topic, primarily at a national level, no consensus appears to be emerging yet. We note that several regulators, including those in the United States, United Kingdom, and Switzerland, have initiated efforts to define measures of audit quality. None of these efforts, some of which are in early stages, have resulted in the identification of a set of indicators that could be used to measure audit quality, as envisaged by the Transparency Consultation. These initiatives have struggled to strike a balance that is sufficiently flexible to work across a range of firms even within a single jurisdiction without becoming mechanical computations of limited value.

We strongly support a dialogue with audit oversight bodies and regulators on audit quality indicators. However, we believe that substantial further work is required before a generally accepted set of audit quality indicators can be defined and then used as a benchmark to measure audit quality effectively. Items that we believe should be considered include a discussion of audit quality drivers such as tone at the top, internal quality control systems including inspection and an overview of training and continuing education requirements. We would be pleased to draw on our experience in the area to assist in any such dialogue.

The examples of input and output measures provided in the Transparency Consultation each can be argued to have some link to audit quality, either directly or indirectly. Items that we believe have strong links to audit quality are tone at the top, internal quality control systems including inspection

⁹ Auditor liability reform should take the form of proportionate liability, in combination with a mechanism that limits absolute exposures. Subject to this, policy makers should have flexibility to establish liability limitations with regard to both public interest considerations and the interests of all market participants. We believe that this solution serves the public interest because it properly allocates damages among those at fault, reduces the likelihood of catastrophic claims against audit firms, addresses fairly a plaintiff’s right of redress, and reduces the risk of further concentration in the larger public company audit market.

¹⁰ See London Economics study, above and the European Commission Recommendation of 5/VI/2008 concerning the limitation of the civil liability of statutory auditors and audit firms.

¹¹ Objective parties that have looked at this question agree that public disclosure of audit firm financial statements would not enhance competition and/or audit quality. See, e.g., the U.S. Government Accountability Office (GAO) January 2008 report on concentration in the auditing profession, which observes that “[m]ost market participants we interviewed on this proposal did not believe that requiring audit firms to publicly disclose their financial results would be very effective in reducing the risk of anticompetitive pricing among the largest accounting firms”. Available at <http://www.gao.gov/new.items/d08163.pdf> (page 54).

and training, and continuing education requirements. Once relevant measures are identified, the next steps are establishing consistent methods of deriving these quantitative measures and establishing norms against which an individual firm's performance can be compared. The final step is to find a way to communicate the audit quality indicators in a manner that will be understood clearly by third parties.

Another complicating factor is that the significance of such measures with respect to audit quality will, in practice, vary significantly from jurisdiction to jurisdiction depending upon factors that include the nature and complexity of the audit practice, the entities audited, the industry sectors, the stability or degree of change in applicable audit and financial reporting standards, the economy, technology etc. Benchmarks for output measures, in particular, may be difficult to determine and their link to audit quality more difficult to establish; measurement also may be more difficult to agree if the items being measured are more subjective by nature.

We believe that for indicators to be effective they first must be found to be directly relevant to the audit firm. In other words, audit quality indicators must be useful to the individual firm itself in assisting in monitoring and measuring audit quality. We also believe that once a set of indicators has been identified and agreed as being relevant to a specific practice (taking account of size, factors specific to the firm's jurisdiction, etc.) the initial use of such indicators should be for constructive dialogue with qualified, informed bodies such as audit oversight bodies and market regulators. Confidential discussions between an audit firm and its audit oversight regulators would provide the context necessary to assess the validity of the findings as measures of quality – for example, whether the measures are consistent or inconsistent with the findings in engagement examinations. We believe that broader use – e.g. public disclosures – of audit quality indicators should not be mandated until they have been reviewed and perhaps refined drawing on this experience.

* * * * *

KPMG is a global network of member firms working in diverse countries with overlapping and at times inconsistent regulatory requirements. We applaud efforts by IOSCO and its members to both enhance and rationalise regulatory requirements in order to support increasingly global capital markets. Consistent regulatory requirements support our commitment to quality and global consistency in the application of high quality international auditing and accounting standards. We look forward to contributing to any further work in this area.

In responding to questions posed by IOSCO in the Transparency Consultation we have focused on those that are most relevant to audit firms and networks as we believe that some questions are more relevant for other stakeholders. Our responses to selected questions are given in an appendix to this



letter. We would be very happy to discuss any of these points further; if you have any questions then please contact Dr Wienand Schruoff, Head of Global Regulatory Issues, at +4930 2068 1480.

Yours sincerely

KPMG International

KPMG International

Appendix 1 – responses to selected IOSCO questions

II. Possible Effects of Transparency related to Audit Quality and Availability and Delivery of Audit Services

Is a definition of audit quality necessary to evaluate audit quality or can audit quality be evaluated from an understanding of the attributes, behaviours, and indicators of audit quality?

We believe that lack of an agreed definition of audit quality indicators should not be a barrier to effective disclosures of audit firm transparency that support an evaluation of efforts to drive audit quality. As discussed in our cover letter under “KPMG Supports Transparency” we believe that Article 40 is an appropriate framework on which to base requirements for public transparency disclosures. We believe that public transparency disclosures should provide insight into an audit firm’s structure and governance systems, and its controls and procedures that are drivers of audit quality.

We strongly support a dialogue with audit oversight bodies and regulators on audit quality indicators. However, we believe that substantial further work is required before a universally accepted set of audit quality indicators can be defined and then used as a benchmark to measure audit quality effectively. See the discussion in our cover letter under “Audit Quality Indicators”.

In addition to competence and industry expertise of the audit personnel, firm culture that promotes audit quality, firm-wide quality control systems, and auditor oversight, are there other examples of attributes, behaviours, and indicators of audit quality that should be considered?

It is helpful to have an inventory of factors that can influence and/or provide evidence for audit quality such as the discussion provided in the IOSCO paper. However, we believe that such a discussion should be used as a memory jogger rather than a mandated list of items to be addressed in a transparency discussion.

III. Transparency of Audit Firms' Governance

Are there other areas of governance for which additional transparency should be considered?

We believe that the four areas identified by IOSCO – network governance structure and management of audit firms; quality control systems; human resources, including training; and independence and ethics – are all relevant aspects for a firm or network to address in its transparency disclosures. As discussed in our cover letter under “Principles for Transparency Disclosures” we believe that some of the specific items canvassed within these categories are not appropriate requirements, e.g., insurance and liability arrangements.

Would the proposed disclosures mentioned above be useful in improving audit quality and availability and delivery of audit services to public companies?

We believe that stakeholder and public understanding of the audit and of measures that firms take to enhance audit quality strengthens the capital markets by instilling public confidence in audited financial statements. We welcome efforts by capital markets regulators and others to broaden discussions about auditor competition and choice so that there is reinforcement for those responsible for auditor appointments to consider not only cost but also audit quality.

As noted in our cover letter under “Principles for Transparency Disclosures” we believe that some of the specific disclosures considered could have the unintended impact of reducing rather than expanding choice in some circumstances depending on the legal and liability climate in the jurisdiction.

Could other limitations arise if such disclosures were required?

Public disclosure of liability and insurance arrangements not only could increase the exposure of audit firms to more and greater claims by third parties but also reduce the availability of insurance for larger claims. We refer you to the conclusions reached by the London Economics report on auditor liability that was commissioned by the European Commission; see “Principles for Transparency Disclosures – Insurance and liability arrangements”.

IV. Transparency of Audit Firms' Audit Quality Indicators

Can audit quality indicators provide objective information when evaluating a firm's audit quality? If so, do the ones identified in this report accomplish that goal?

As discussed in our cover letter under the heading "Audit Quality Indicators" we strongly support a dialogue with audit oversight bodies and regulators on audit quality indicators.

In addition to the benefits or limitations identified in this report, are there any other benefits or limitations about disclosing audit quality indicators that need to be considered?

We support a dialogue on audit quality indicators; see the discussion in our cover letter under "Audit Quality Indicators."

V. Transparency of Audit Firms' Financial Statements

Can audited financial statements of audit firms provide useful or objective information regarding audit quality? If so, how?

As noted above in our response to Question 4 and in our cover letter, while a number of KPMG member firms publish financial statements, others do not in light of the legal and liability environment. While financial statements of audit firms may be relevant to oversight authorities in discharging their responsibilities, we are not aware of any evidence, nor do we see the possibility, that publication of financial statements contributes in any way to audit quality. In our view, audit oversight authorities generally have access to the financial and other types of information that they feel is necessary to fulfil their oversight obligations. See the discussion in our covering letter under the heading "Principles for Transparency Disclosures – Financial statement disclosure".

If disclosure to the public or regulators of an audit firm's own audited financial statements is warranted, who should audit the auditors? Are firms other than the Big Four equipped to audit the Big Four? If not, does having the Big Four firms audit each other raise concerns? If so, then how could any such concerns be addressed?

The financial statements of the KPMG Europe LLP member firm of KPMG International are audited by Grant Thornton. KPMG Europe LLP identified key concerns for its auditor selection as the ability to carry out audit work effectively on a

cross-border basis and bring to bear expertise in auditing a professional service firm. It concluded that a non-Big Four firm had this capacity and that having a competitor firm conduct the audit did not raise concerns.

The Nordic Federation of Public Accountants

Greg Tanzer
Secretary General
International Organization of Securities Commissions
C/ Oquendo 12
28006 Madrid
Spain

Nordic Federation of Public
Accountants
Kronprinsessegade 8
1306, Copenhagen
Denmark
Telephone +45 33691065
email: jr@nrfaccount.com

By email: AuditorTransparency@iosco.org

15th January 2010

Public Comment on the Transparency of Firms that Audit Public Companies: Consultation Report

The Nordic Federation of Public Accountants (NRF) is pleased to comment on IOSCO's Consultation Report, *Transparency of Firms that Audit Public Companies* ("Consultation Report"). NRF refers to, and is responding on behalf of, the recognised accounting bodies in the Nordic region (Denmark, Finland, Iceland, Norway and Sweden). Each accounting body in the region is autonomous and consequently may also chose to respond individually to IOSCO's Consultation Report. The views expressed in this letter do not in any way commit or restrict the positions of any individual member bodies of NRF. However, the views expressed in this letter have been reviewed by NRF's member bodies and are generally consistent with the views of these member bodies, each of which is a separate legal entity.

As an organisation NRF is committed to promoting the consistent application of high quality audit and accounting practices within the Nordic region as well as worldwide, in the public interest and welcomes initiatives designed to advance these objectives and to encourage greater participation by more recognised accountants and accounting firms in the public company audit market.

NRF supports transparency about all issues relevant to audit quality. Transparency regarding matters that affect audit quality contributes to the effective operation of global capital markets and NRF supports the provision of relevant and appropriate disclosures to oversight authorities and other stakeholders to enhance stakeholder understanding of the audit process and related reporting.

NRF's main comments are as follows:

- NRF supports independent regulation and audit oversight and recognises that independent audit oversight should result in full transparency to the regulator and that the regulator has certain important confidentiality obligations.
- One of the functions of the independent audit regulator is to provide assurance to the capital markets of recognised auditors and audit firms' independence and integrity, as well as audit quality.
- Transparency to other stakeholders could be on the basis of providing information on the grounds for choosing an auditor. It is the role of the audit committee to make recommendations on the choice of auditors. Where audit committees exist and are properly embedded in a recognised governance structure, auditors and audit firms are fully transparent and provide audit committees with the information they require on the assumption that obligations of confidentiality are upheld.

NRF

- NRF believes that a constructive framework for transparency disclosures can be based on the reporting regime required by Article 40 of the European Union's Company Law Directive on Statutory Audits and that this framework currently provides a useful and sufficient global benchmark for transparency disclosures to investors and other stakeholders.

NRF's views are elaborated on below and are also incorporated in the specific requests for consultations numbered 1 to 20 which follow thereafter.

Oversight of recognised auditors and auditing firms

In recent years, many of the world's most economically significant countries have formed independent audit oversight bodies to regulate auditors. NRF believes that independent audit oversight is an effective means of improving audit quality and increasing confidence in capital markets. NRF supports the creation of independent oversight bodies where they do not exist. Inspection by a capable and independent oversight authority increases the public's trust and confidence in the work of audit firms as well as in capital markets.

Public company auditors and audit firms are highly visible to their audit oversight authorities. It is clear that transparency towards relevant independent oversight authorities plays a significant role in effective oversight of the audit profession and NRF supports such transparency. Audit firms currently provide a wide variety of information to the oversight authorities, by means of the various registration, inspection and reporting processes. Audit firms registered in European Union Member States are required to publicly disclose certain types of firm-wide information. Much of this information is subject to confidentiality and other requirements of the relevant laws and regulations in the EU and Member State jurisdictions. These protections operate to facilitate the supervisory dialogue between oversight authorities and the audit firms thereby enhancing the ability of those oversight authorities to engage in strong and effective oversight of the auditing profession.

Disclosure to Audit Committees and Other Stakeholders

Disclosures to stakeholders other than independent audit regulators should be governed by the objectives of the information stakeholders need to make relevant decisions and the appropriate levels of protection that can be given to sensitive information held by the auditor. As a consequence of this, audit firms are highly transparent with audit committees, who generally are responsible (within the EU at least) for the recommendation for appointment of the auditors to the shareholders. Auditors are able to share a significant amount of useful but sensitive information with audit committee members because there are effective confidentiality rules that protect against the use of such information for other purposes, such as for competitive business advantage or to gain an advantage in litigation.

However, disclosure of certain information relating to the audit firm to investors is important and appropriate because investors rightly need and expect information about the audit firm and audit quality in order to reach an informed judgement about whether to vote for appointment and to consider the performance of their board and audit committee members. However, such disclosure to investors is by nature public information, so the need for transparency with this group of stakeholders must be balanced with concerns about the sensitivity of the information and the damage that can be caused by its issuance.

An Appropriate Model for Public Disclosure

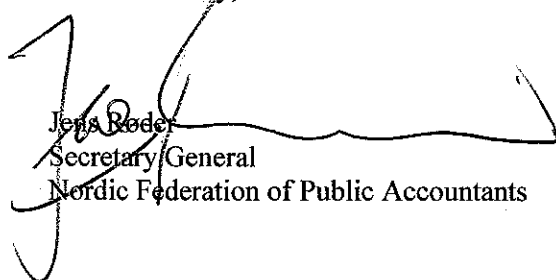
NRF supports the idea of a model for a set of public disclosures that provides information relevant to the needs of the investing public. The Consultation Report identifies Article 40 of the European Union's Company Law Directive on Statutory Audits (Article 40) as a source of information related to governance of audit firms that perform assurance work for public interest entities. NRF believes that Article 40, including its provisions regarding financial information, provides a useful model for a set of transparency disclosures that provides appropriate information for stakeholders.

Many accounting firms in the European Union have already published transparency reports as required by Article 40, and NRF expects that further firms around the world will chose to do so as Article 40 is implemented by more European Union Member States. Thus, the provisions in Article 40, which were agreed after a long process and considerable debate by authorities in Europe, have the greatest prospect of becoming the *de facto* international standard for audit firm transparency reporting and should be the benchmark for the foreseeable future. Investors, audit committees, regulators and other users of this information will gradually increase their familiarity with these disclosures and, on that basis, the effectiveness of these disclosures can be further analyzed to improve the information to stakeholders concerning audit quality.

Any proposed disclosures beyond those included in the Article 40 framework should be considered only if it is clear that the provision of additional information contributes to increase the understanding of audit quality. The inherent limitations of various disclosures should be considered. The concept of audit quality is subjective in nature and is therefore subject to different interpretations with the potential for negative consequences that this may lead to if unreliable conclusions are drawn from the information. For example disclosures related to additional financial information, insurance arrangements and the availability of insurance, independence violations, and legal proceedings against audit firms may impact litigation risk. This could contribute to the risk of future collapse of an existing firm and lead to further market concentration. This risk should be evaluated against the contribution such disclosures might have, if any, to a better understanding of audit quality.

We have addressed below the specific issues raised for consideration in the Consultation Report. We would be pleased to further discuss our comments with you. If you have any questions regarding this letter, please contact Jens Røder at + 45 33691065, email jr@nrfaccount.com.

Yours sincerely,



Jens Røder
Secretary General
Nordic Federation of Public Accountants

REQUEST FOR CONSULTATION:

POSSIBLE EFFECTS OF TRANSPARENCY RELATED TO AUDIT QUALITY AND AVAILABILITY AND DELIVERY OF AUDIT SERVICES

- 1. Is a definition of audit quality necessary to evaluate audit quality or can audit quality be evaluated from an understanding of the attributes, behaviors and indicators of audit quality?**
- 2. In addition to competence and industry expertise of the audit personnel, firm culture that promotes audit quality, firm-wide quality control systems, and auditor oversight, are there other examples of attributes, behaviors, and indicators of audit quality that should be considered?**

NRF welcomes a debate on this question. A definition may be helpful but it should be strongly based on the attributes of how the audit is performed and should itself be of use when developing audit practices. Describing the attributes, behaviours or indicators of audit quality may provide a more appropriate and functional alternative. This could cover factors such as individual country regulations and audit firm cultures as well as global or regional firm-wide quality control systems, the expertise of those involved in audits and the systems of audit oversight, all of which provide indicators of the levels of auditor quality and performance.

When considering such a definition it should be considered that there are many factors affecting audit quality which are outside the control of the individual auditor, the audit firms and the auditing profession. NRF would suggest that the financial reporting infrastructure as a whole should also be considered. This includes accounting standards, auditing standards, the statutory framework for audit and accounting and the system of corporate governance, monitoring and enforcement.

An effective system of corporate governance helps to ensure that the interest of shareholders, as well as the broader public interest, are respected and protected in corporate decisions and actions. An effective and credible system of auditor oversight, including independent inspection of audit quality controls, contributes directly to audit quality. Finally, an effective system of enforcement ensures that all of the participants in the financial reporting process, both organizations and individuals, face the threat of disciplinary action if they act inappropriately.

TRANSPARENCY OF AUDIT FIRMS' GOVERNANCE

- 3. Are there other areas of governance for which additional transparency should be considered?**
- 4. Would the proposed disclosures mentioned above be useful in improving audit quality and availability and delivery of audit services to public companies?**
- 5. Could other limitations arise if such disclosures were required?**

Transparency is an important element underpinning the confidence of the world's capital markets and in creating a more accountable and robust accounting and auditing profession. Audit firms are transparent to independent audit regulators and this enhances audit quality.

In addition to transparency to regulators NRF supports disclosures to the public which are tied to audit quality and contribute to investor confidence and informed decision making by stakeholders. In this regard, a constructive framework for transparency disclosures is the transparency reporting regime required by Article 40 of the European Union's Company Law Directive on the Statutory Audits (Article 40) and that this provides useful information for stakeholders. It includes information on legal structure and ownership of audit firms, governance structure, whether the audit firm belongs to a network, description and structure of the network, independence practices, internal quality controls, quality assurance reviews and continuing education of professionals. It also highlights the attention paid to client acceptance and risk management. It is NRF's belief that the framework provided in Article 40 provides a useful and sufficient global benchmark for transparency disclosures to investors and other stakeholders. Any proposed disclosures beyond those included in the Article 40 framework should be considered only if this provides additional information that is relevant to understanding audit quality.

It should be considered whether the potential costs and unintended consequences of additional disclosures outweigh the benefits. Therefore, any consideration of additional disclosures beyond those in the Article 40 framework should be carefully studied and analyzed against the criteria of audit quality enhancement and stakeholder utility.

TRANSPARENCY OF AUDIT FIRMS' AUDIT QUALITY INDICATORS

- 6. Can audit quality indicators provide objective information when evaluating a firm's audit quality? If so, do the ones identified in this report accomplish that goal?**
- 7. In addition to the indicators identified in this report, are there any other audit quality indicators that should be considered for disclosure? Would disclosure of the audit quality indicators described above be helpful in evaluating audit quality?**
- 8. In addition to the benefits or limitations identified in this report, are there any other benefits or limitations about disclosing audit quality indicators that need to be considered?**

The Consultation Report discusses whether specific audit quality indicators, either qualitative or quantitative, should be developed with the aim of providing investors and other stakeholders with "objective information" that may help them to evaluate audit quality. NRF understands and supports the need for transparency of useful information to allow participants in the capital markets to make measured auditor selection decisions. Audit firms already provide comprehensive information about their internal operations to their oversight authorities. This transparency contributes to audit quality. Independent oversight and inspections contribute to the credibility of published financial information and the protection of stakeholders who use it. The inspection process is an important tool in maintaining and enhancing quality over audits. NRF believes that any transparency proposals should be evaluated based on whether they enhance audit quality, balanced against possible unintended negative consequences. This includes any considerations regarding the publication of audit quality indicators.

Greg Tanzer
Secretary General
International Organization of Securities Commissions
C/ Oquendo 12
28006 Madrid
Spain

By email: AuditorTransparency@iosco.org

January 15, 2010

**Public Comment on the Transparency of Firms that Audit Public Companies:
Consultation Report**

PricewaterhouseCoopers ("PwC") is pleased to comment on IOSCO's Consultation Report, *Transparency of Firms that Audit Public Companies* ("Consultation Report"). PwC refers to, and we are responding on behalf of, the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate legal entity. As a network we are committed to promoting the consistent application of high quality audit practices worldwide in the public interest and welcome reasonable initiatives designed to advance these objectives and to encourage greater participation by more accounting firms in the largest public company audit market.

PwC supports transparency about issues relevant to audit quality. We recognize that transparency regarding matters that affect audit quality contributes to the effectiveness of the global capital markets and we support providing appropriate disclosures to both oversight authorities and other stakeholders to enhance stakeholder understanding of the audit and the measures that firms take to enhance audit quality and confidence in financial reporting.

Our comments highlight the following points:

- PwC supports independent regulation. Where there is independent audit oversight the regulator in the jurisdiction has a critical role to play in promoting audit quality, and in enhancing the reliability of publicly reported financial information.
- As public company auditors, we also understand and support the need for transparency of useful information which would allow participants in capital markets to make sound and measured auditor selection decisions.

- Therefore, transparency to stakeholders other than regulators should be in the context of providing information relevant to choosing an auditor. Just as public companies seek to attract investors through strong financial results, audit firms should seek to distinguish themselves on the basis of measures of audit quality.
- With this in mind, it is our view that the reporting regime required by Article 40 of the European Union's Eighth Directive and the framework this provides is a useful and sufficient global benchmark for transparency disclosures to investors and other stakeholders. It is important to carefully consider the benefits or other effects, to investors or other stakeholders, of these disclosures over time so as to minimize unintentional consequences.

Our views are discussed further below and are also incorporated in the IOSCO's specific requests for consultations under the Consultation Report's chapter headings which follow thereafter.

Oversight of Auditing Firms by Home Country Oversight Bodies

In recent years, many of the world's most economically significant countries have formed independent oversight bodies to regulate auditors. We believe that independent oversight is an effective means of improving audit quality, and we support the creation of independent oversight bodies where they do not exist. Inspection by a capable and independent oversight authority in the audit firm's jurisdiction(s) increases the public's trust and confidence in the work of audit firms and provides an important safeguard to audit quality and independence.

Public company audit firms are highly visible to their audit oversight authorities. In most instances, these oversight bodies obtain broad, unencumbered access to public company audit firm proprietary information, which we believe is necessary for the body charged with maintaining the quality of audits performed by private entities that are not subject to public reporting. The Public Company Accounting Oversight Board (PCAOB) in the United States and regulators in other countries have virtually open access to proprietary information about public accounting firms through their inspection functions. Much of this information is subject to confidentiality and other requirements of the relevant laws and regulations in the relevant jurisdiction(s). These protections operate to facilitate the supervisory dialogue between oversight authorities and the audit firms thereby enhancing the ability of those oversight authorities to engage in strong and effective oversight of the profession.

Disclosure to Audit Committees and Other Stakeholders

Disclosures to stakeholders other than regulators are, and should be, driven by measures of audit quality and by the objectives of the information stakeholders need to make relevant decisions, balanced by the levels of protection appropriate for sensitive information. Thus audit firms provide audit committees with meaningful information to allow participants to make sound and measured auditor selection decisions, benefiting those who (depending on the jurisdiction) either appoint the auditors or recommend their appointment to the shareholders. Audit firms are able to share a significant amount of useful but sensitive information with audit committee members because there are effective protections in place that prevent the use of such information for other purposes, such as for competitive business advantage or to gain an advantage in litigation.

Disclosure of certain information to investors may also be important and appropriate because investors need and expect information about the audit firm and its audit quality in order to reach an informed judgement about whether to vote in favour of its appointment, as well as to consider the performance of the audited company's board and audit committee members. However, any disclosure to investors will by nature become public information so investors' need for transparency should be balanced with the risks identified below.

An Appropriate Model for Public Disclosure

We support the idea of a model for a set of public disclosures that provides information relevant to the needs of the investing public. The Consultation Report identifies Article 40 of the European Union's Eighth Company Law Directive as a source of information related to audit firms that perform assurance work for public interest entities. We believe that Article 40 of the Directive, including its provisions regarding financial information, provides a useful model for a set of transparency disclosures that provides appropriate information for stakeholders.

Many audit firms already publish transparency reports as required by Article 40, and we expect that additional firms around the world will do so as third country auditor registration requirements are implemented by more European Union Member States. Thus, we consider that Article 40, agreed after a long process and considerable debate by authorities in Europe, has the greatest prospect of becoming the *de facto* international standard for audit firm transparency reporting and should be the benchmark for the foreseeable future. It is important for investors, audit committees, regulators and other

users of Article 40 transparency reports to have sufficient time to become more familiar with these disclosures and their effectiveness. Disclosures can then be further analyzed to determine whether changes to the requirements are needed to appropriately inform stakeholders about audit quality.

Any proposed disclosures beyond those included in the Article 40 framework should be considered only if they would provide additional information that is both relevant to understanding audit quality and useful to and understandable by stakeholders. We question whether additional disclosures beyond those included in Article 40 would be helpful to stakeholders. The inherent limitations of various disclosures should also be considered, including the subjective nature of the concept of audit quality and the potential for negative consequences, including whether unreliable conclusions can be drawn from the information. For example disclosures related to financial information, insurance arrangements and amounts, independence violations, and legal and regulatory proceedings may impact a firm's litigation risk. Increases in litigation risk may, in turn, increase the risk that an existing firm might collapse which would lead to further market concentration. As this example demonstrates, the potential contribution (if any) of disclosures to an understanding of audit quality should be weighed against the potential risks.

We have addressed below the specific issues raised for consideration in the Consultation Report. We would be pleased to further discuss our comments with you. If you have any questions regarding this letter, please contact Kenneth R. Chatelain at + 1 202 312 7740.

Sincerely,



PricewaterhouseCoopers

REQUEST FOR CONSULTATION:

**POSSIBLE EFFECTS OF TRANSPARENCY RELATED TO AUDIT QUALITY
AND AVAILABILITY AND DELIVERY OF AUDIT SERVICES**

Questions 1 and 2 address issues regarding the need for a definition of audit quality and indicators of audit quality. PwC welcomes further debate on this issue. We would suggest that a definition may be helpful but there is a chance that it could be counterproductive. We believe it would be more appropriate and useful to consider the attributes and behaviours that contribute to audit quality, as these take into account such factors as firm culture, firm-wide quality control systems, the expertise of those involved in audits, and the system of audit oversight, all of which provide assessments of auditor performance.

We have not, so far, seen a definition of audit quality that we have found satisfactory. Ideally, a definition should be based on outputs but assurance of financial reporting as a whole is outside the control of audit firms and the auditing profession. In considering the outputs of audit quality, the financial reporting infrastructure as a whole should be considered, including accounting standards, auditing standards, the statutory framework and system of corporate governance, monitoring and enforcement. An effective system of corporate governance helps to respect and protect the interest of shareholders, as well as the broader public interest, in the context of corporate decisions and actions. An effective and credible system of auditor oversight, including independent inspection of audit firm quality controls, contributes directly to audit quality, particularly when coupled with an effective system of enforcement so that all of the participants in the financial reporting process, both organisations and individuals, face disciplinary action if they act inappropriately.

TRANSPARENCY OF AUDIT FIRMS' GOVERNANCE

Questions 3 to 5 address whether there are areas of governance for which additional transparency should be considered, if this would affect audit quality and delivery of audit services and if there are limitations to disclosure.

We believe transparency is an important element underpinning the confidence of the world's capital markets and in creating a more accountable and robust accounting profession. Audit firms' transparency with their regulators enhances audit quality. In addition to transparency to regulators, as noted earlier, we support disclosures to the public which are both tied to audit quality and contribute to investor confidence and informed

decision making by stakeholders. We believe that Article 40 of the European Union's Eighth Directive provides useful information for stakeholders and therefore is a constructive framework for transparency disclosures. Under Article 40, an audit firm is required to disclose legal structure and ownership, governance structure, whether the firm belongs to a network (including a description of the structure of the network), independence practices, internal quality controls, quality assurance reviews, and continuing education of professionals. The Article 40 disclosures also highlight the attention the audit firm pays to client acceptance and risk management. Given the scope of disclosures required under Article 40, and the information they provide relevant to audit quality, it is our belief that the Article 40 framework provides a useful and sufficient global benchmark for transparency disclosures to investors and other stakeholders.

Any proposed disclosures beyond those included in the Article 40 framework should be carefully studied and analyzed against the criteria of audit quality enhancement and stakeholder utility. Only if a disclosure would provide additional information that is relevant to decision making by recipients and understanding audit quality should it be adopted, provided that potential benefits outweigh the potential costs and unintended consequences of additional disclosures. For example, we question whether additional disclosures regarding the non-audit practice of an audit firm, financial information beyond that required under Article 40, or detailed disclosures related to engagements would be helpful to stakeholders and whether such benefits would be outweighed by potential costs.

TRANSPARENCY OF AUDIT FIRMS' AUDIT QUALITY INDICATORS

Questions 6 to 8 examine whether audit quality indicators provide objective information in evaluating a firm's audit quality and if disclosure of audit quality indicators are helpful in evaluating audit quality and what the benefits or limitations are.

The Consultation Report discusses whether specific audit quality indicators, either qualitative or quantitative, should be developed with the aim of providing investors and other stakeholders with "objective information" that may help them to evaluate audit quality. We understand the need for transparency of useful information to allow participants in the capital markets to make measured auditor selection decisions. Audit firms provide their oversight authorities with significant transparency into their internal operations, to facilitate the oversight and inspection process. Oversight and inspections achieve the overarching goal of adding credibility to published financial information and protection to the stakeholders who use it and the inspection process is an important tool in maintaining and enhancing quality over audits. We believe that transparency proposals should be evaluated based on whether they enhance audit quality.

The selective use of audit quality indicators could increase the risk of litigation for audit firms, particularly in the United States because of its securities class action climate, as well as other countries. Increased litigation risk could negatively impact audit firms' viability in certain jurisdictions because of high exposure within the legal system. It is important to note that risk of litigation is not only a problem for the larger firms; it also deters small and mid-sized firms from expanding their public-company audit business or entering the market in the first place.

The framework included in Article 40 of the EU Eighth Directive provides the most appropriate model for transparency disclosures as explained in our opening comments.

TRANSPARENCY OF AUDIT FIRMS' FINANCIAL STATEMENTS

Questions 9 through 11 address issues related to firm financial information including audit firm financial statements and whether that information is useful to an assessment of audit quality.

While we recognise that audit firms in some countries are required to provide financial statements this is generally a consequence of adopting a limited liability structure and applies to all businesses with that structure, rather than only to audit firms.

We do not believe public financial statements of audit firms are relevant to understanding an audit firm's audit quality. For example, it is impossible to tell from financial statements whether a firm that shows low profits does so because it is poorly organised or because it spends more time delivering the highest quality. The costs of providing such information may also be very high in some jurisdictions, such as the United States with its liability climate and potential for bringing class actions. Moving towards possibly providing detailed audit firm financial information, either in the form of financial statements or other information, for access by those asserting claims would be detrimental to the goals of sustainability and competition. We believe that preparation and submission of audited financial statements for audit firms may impose a significant burden on audit firms without any concomitant enhancement in audit quality and that greater public disclosure could harm rather than improve competition in a way that would outweigh any correlation of firm financial results to audit quality.

Financial disclosure for public companies is necessary as a means for their owners to understand and monitor how companies are performing. For audit firms the equivalent disclosure would involve metrics that provide the capital markets with confidence that audit firms are providing trustworthy, quality audits. It is our belief that there is no compelling reason that disclosure of audit firm financial statements, or other financial information, would enhance audit quality. Companies seek access to capital and potential investors need sound, reliable financial information and reporting to make investment

decisions. This rationale does not apply to accounting firms as they are owned by their partners. Public companies wishing to make informed choices about auditor quality and competence would not be better informed by having access to the financial statements of accounting firms and there is no evidence that there is a desire in the capital markets for proprietary firm financial information.

To the extent that the capital markets require assurance about public company auditor soundness regulators have authority to request such information as deemed necessary to the performance of their oversight functions and to determine audit quality.

PARAMETERS OF ENHANCED DISCLOSURE FOR AUDIT FIRMS

Questions 12 to 16 address considerations for further transparency disclosures, what these may comprise and by whom they should be provided.

We support disclosures in line with the framework of Article 40 of the EU Eighth Directive inasmuch as they have a connection to enhanced audit quality. As previously noted many audit firms have already published transparency reports as required by Article 40, and we expect that additional audit firms around the world will do so as Article 40 is implemented further. Any disclosures beyond those contained in the Article 40 framework should be considered only if doing so would provide additional information that is relevant to decision making by stakeholders and we believe that careful study and analysis should first be made. Requirement for additional disclosures should be based only on a compelling connection, which at this point we do not believe there is, to enhanced audit quality. In any event we question whether additional disclosures involving information about the non-audit practice of the firm and financial information beyond that included in Article 40, and detailed disclosures related to engagements would meet these criteria and be helpful to stakeholders.

The overall function of audit oversight serves to enhance audit quality. Disclosures provided to oversight bodies by audit firms perform the function of enhancing audit firm oversight and thereby confidence in audit quality. Transparency does not mean that everything should be publicly disclosed. Disclosure of audit firm financial statements to the public would not enhance audit quality and provide no materially useful information to capital markets participants. To the extent that the capital markets require assurance about public company auditor soundness, regulators have authority to request such information as deemed necessary to the performance of their oversight functions and to determine audit quality. Information is more relevant to regulators and we do not believe that there should be public disclosure for its own sake. Furthermore, having certain public information available, for example regarding pending litigation, could be detrimental to the parties involved.

All public company audit firms should be subject to the same disclosure requirements irrespective of the size of the firm, i.e., requirements should apply to large, mid-size and small audit firms alike for the reason that audit firms that fall outside the reporting regime may face the problem of the false impression that lack of disclosure means they are less well-regulated than the larger firms. Such a bias has the potential to undermine the efforts of small and mid-size firms to attract and retain clients. The costs and benefits of additional disclosures should be analysed in general and particularly as they relate to the smaller and mid-sized firms who may consider that additional disclosures are too costly and elect not to enter a market segment.

SUMMARY

Questions 17 to 20 address whether transparency of audit firms would improve audit quality and the availability and delivery of audit services, whether this would lead to benefits to investors and increased investor confidence and if additional areas of disclosure should be considered. As we noted earlier, audit firms provide their regulators with significant access to information about their internal operations and processes and regulators have the authority to request such information as they deem necessary to perform their oversight functions and to assess audit quality. Regulators operate on behalf of the investing public and other stakeholders to provide confidence in the reliability of financial reporting. Because of their professional obligations and legal and reputation risks, audit firms have significant incentive to focus on audit quality. Regulator oversight reinforces this existing incentive. We do not believe that transparency in and of itself serves to enhance audit quality. Likewise, we do not believe that disclosures in and of themselves will enhance competition or concentration in the market for auditing the largest public companies. We support narrative disclosures linked to enhancement of audit quality in line with those in the Article 40 framework, rather than audit quality indicators or metrics which do not directly correlate with enhancing audit quality. Accordingly we believe that Article 40 provides a sufficient benchmark.

There is debate regarding the link, which has not been demonstrated, between issuing audited financial statements or other financial information and enhancement of audit quality. Investors invest in companies not audit firms. Financial information for public registrants is necessary as a means for investors and owners to understand and monitor performance. For audit firms the equivalent disclosure would involve information that provides the capital markets with confidence that audit firms are providing trustworthy, quality audits. It is our belief that there is no compelling connection that additional disclosures by audit firms would fulfil the purpose of enhanced audit quality. Companies seek access to capital and potential investors require reliable financial

information and reporting to make investment decisions. This rationale does not apply to accounting firms as they are owned by their partners.

Selective use of audit quality indicators could also increase the risk of litigation for audit firms, particularly in the United States, as well as other countries which, because of exposure within the legal system, could have negative consequences on an audit firm's viability in certain jurisdictions. The risk of litigation is not only a problem for the larger firms; it also deters small and mid-sized firms from expanding their public-company audit business or entering the market in the first place.

SEC Thailand

Transparency of Firms that Audit Public Companies

Consultation Report

Questions	Comments
POSSIBLE EFFECTS OF TRANSPARENCY RELATED TO AUDIT QUALITY AND AVAILABILITY AND DELIVERY OF AUDIT SERVICES	
1. Is a definition of audit quality necessary to evaluate audit quality or can audit quality be evaluated from an understanding of the attributes, behaviors, and indicators of audit quality?	We believe that both the definition of audit quality and the understanding of the attributes, behaviors, and indicators of audit quality are necessary to evaluate audit quality. The definition of audit quality is required for standardizing understanding of each audit firm in developing their audit quality in the same direction. This also ensures the consistency and comparability of information disclosure about audit quality. If there is no specific and clear definition of audit quality, audit firms may be influenced to select only their positive results to disclose. The understanding of the attributes, behaviors, and indicators of audit quality are also important to evaluate audit quality because these characteristics can be used to measure the audit quality level of audit firms.
2. In addition to competence and industry expertise of the audit personnel, firm culture that promotes audit quality, firm-wide quality control systems, and auditor oversight, are there other examples of attributes, behaviors, and indicators of audit quality that should be considered?	<p>The examples of attributes, behaviors, and indicators of audit quality that should be considered are as follows;</p> <ul style="list-style-type: none"> - Results from the compliance test of audit quality control system (both from internal monitoring procedures or from regulator inspections) - Statistics of financial misstatements - Insurance premium (it should reflect risk and quality of each audit firm) - Salary and other compensation of partner - Non-audit fees compared to audit fees (indicator of conflict of interest) - Audit firms' governance, core value, code of conduct, and policy and procedure - Statistics of late submission of work to clients - Turnover of senior employees and management - Significant changes in audit fees compares to the previous year of the same client (very low/high audit fee may reflect quality of work and input resource/ audit risk)
TRANSPARENCY OF AUDIT FIRMS' GOVERNANCE	
3. Are there other areas of governance for which additional transparency should be considered?	<p>There should be audit firms' procedures to monitor that firms and their employees are complied with the following policies;</p> <ul style="list-style-type: none"> - Partners and key persons of audit teams rotation - Firm and employees' confirmation of independence - Integrity of the audit clients which audit firms accepted to render services - Disclosure and transparency of audit firms

Questions	Comments
4. Would the proposed disclosures mentioned above be useful in improving audit quality and availability and delivery of audit services to public companies?	Yes, the mentioned disclosures are useful; however, the disclosure aspects should be consented by regulators to ensure that they are standardized, useful and explicit which should assist the evaluation of the audit quality and availability and delivery of audit services. Additionally, the regulator should monitor the disclosure to ensure the information is truthful and accurate. Besides, the disclosure about governance should help improving audit quality as it is one of the market mechanisms to pressure audit firms to uplift their quality.
5. Could other limitations arise if such disclosures were required?	The limitation of the disclosures may consider in terms of their cost versus benefit, resource's of small audit firms, and negative effects that may occur from the disclosures such as, audit firms' know-how, confidential issue of business, complete advantages.
TRANSPARENCY OF AUDIT FIRMS' AUDIT QUALITY INDICATORS	
6. Can audit quality indicators provide objective information when evaluating a firm's audit quality? If so, do the ones identified in this report accomplish that goal?	Yes, some audit quality indicators provide objective information for evaluating audit firms' quality, especially restatements and inspection results because an error in auditing reflect an audit firm's quality and it can be implied that this audit firm has deficiencies in their quality control systems according to the International Standard on Quality Control (ISQC1). However, some indicators may not directly correlate with audit quality such as revenue of audit firms.
7. In addition to the indicators identified in this report, are there any other audit quality indicators that should be considered for disclosure? Would disclosure of the audit quality indicators described above be helpful in evaluating audit quality?	Other audit quality indicators are as follows; <ul style="list-style-type: none"> - Average salary (include other benefits) of audit staff compares to the industry salary data (in the same level): based on the assumption that firms with high average salary should have more competent staff, hence, those firms should have higher audit quality. - Profit margin of each engagement - Client retention ratio - Results from the compliance test of audit quality control system - Statistics of financial misstatements - Insurance premium (should reflect risk and quality of each audit firm)
8. In addition to the benefits or limitations identified in this report, are there any other benefits or limitations about disclosing audit quality indicators that need to be considered?	Another benefit is a reducing in audit firms' risks as the disclosure and transparency processes help identifying the deficiency and correct it beforehand. Another limitation is the competitive advantages or disadvantages of audit firms to use of disclosure channel as marketing tools.
TRANSPARENCY OF AUDIT FIRMS' FINANCIAL STATEMENTS	
9. Can audited financial statements of audit firms provide useful or objective information regarding audit quality? If so, how?	We believe that the disclosure of audited financial statements provides useful information regarding audit quality because some information can be used to evaluate audit quality for example; high overdue audit client receivable can used to evaluate independent issue. Net income and gross profit margin can be use to determine efficiency and capability of audit firms. However, the uses of financial statements information may be limited because this information

Questions	Comments
	usually does not directly correlate with audit quality so by using this information alone cannot evaluate the quality of audit firms; therefore, this information have to be used to analyze with other parameters, for example, audit quality cannot be evaluated from only significant changes in revenue or profit margin but other factors and detail information are needed to collect for the analysis such as the comparison of revenue compare to input resource per engagement.
10. If disclosure to the public or regulators of an audit firm's own audited financial statements is warranted, who should audit the auditors? Are firms other than the Big Four equipped to audit the Big Four? If not, does having the Big Four firms audit each other raise concerns? If so, how could any such concerns be addressed?	We believe that independent auditors are able to audit financial statements of audit firms because the auditing business is not complex so independent auditors who are qualify as certified public accountants should have capability to audit Big Four and other audit firms.
11. Can disclosing certain financial information instead of audited financial statements achieve the same objective of improving audit quality and the availability and delivery of audit services? If so, what financial information should be disclosed?	<p>We believe that the disclosures of certain financial information instead of audited financial statements can achieve the same objective of improving audit quality and the availability and delivery of audit services. The certain financial information that important for evaluation are as follows;</p> <ul style="list-style-type: none"> - Overdue audit clients receivable - Revenue and profit merging by service lines
PARAMETERS OF ENHANCED DISCLOSURE FOR AUDIT FIRMS	
12. Are there other parameters that should be considered?	<ul style="list-style-type: none"> - Number of Certified Public Accountants and experts within the firms - Number of average hours that audit staff used in learning and development themselves (by position/level) - Average educational degree of audit staff (by position/level) - Career path that audit firms can provide to their audit staff as it should motivate the staff to endeavor work with that firm.
13. Should certain disclosures not be publicly available and if so, what criteria should be considered when determining what disclosures should be publicly available?	We support that the disclosures should be publicly available except the information that may lead to competitive advantages or disadvantages and information that reveals marketing strategies, sensitive or confidential information such as average salary (include other benefits) of audit staff.
14. Should certain disclosures be made at the network, firm, and/or, engagement level?	<p>We believe that the disclosures at firm level are the most important; however, the need of detail information may depend on the evaluation objectives.</p> <p>The information at engagement level may be needed by regulators for further analysis; however, the regulator can obtain this information during the inspection processes. Some detail information may be confidential so it should not be disclosed to the public.</p>
15. Should there be different disclosure requirements for large, mid-size, and small audit	No, regardless the audit firms' size, we believe that the minimum disclosure requirements should be uniform in order that the information can be comparable and consistent.

Questions	Comments
firms?	
16. Should the disclosures be mandatory and if so, should they be subject to regulatory oversight? Would a similar impact to the markets occur if the disclosures were encouraged instead of being mandatory? Should consideration be given to a framework of audit quality and allow for flexibility in the types of disclosures?	<p>We believe that the disclosures should be voluntary, however, if audit firms desire to disclose their transparency report, they must at least disclose standard information that is mandatory and subject to regulatory oversight in order to ensure that all information are accurate and reliable. If the disclosures are free-form, audit firms can maneuver their results by select only favorable information to disclose. Since audit firms are very important for the capital market, standardized public disclosures are necessary for enhancing investors' confidence.</p> <p>Besides, although the disclosures are voluntary, we believe that in long term, market mechanism should drive all audit firms to disclose their transparency report as this is a channel for audit firms to communicate about their quality and governance to their prospective or current clients.</p> <p>The framework and minimum disclosure requirements should be set, however, there should have flexibility for audit firms to disclose further useful information (which is subject to be reviewed by the regulators) and the disclosure format should be flexible.</p>
17. Would transparency of audit firms improve audit quality and the availability and delivery of audit services? What negative effects, including costs, of increased transparency should regulators consider?	<p>Yes, transparency of audit firms should improve audit quality and the availability and delivery of audit services. If the audit firms are more transparent, they should discover potential problems and prevent or correct them promptly and bring about audit quality and investors' confidence in financial reporting. The transparency of audit firms also increases confidence on the availability and delivery of audit services because the important information about audit services can be assessed and evaluated by clients.</p> <p>The negative effects that regulators should consider are costs of increased transparency and confidentiality of information disclosures. Audit firms may have extra costs to increase transparency; however, in the long term they should gain more income to compensate those costs from increasing reliability on their audit quality.</p> <p>Some information disclosure may lead to competitive advantages or disadvantages for audit firms so regulators should consider the effect of the public information and avoid the use of disclosure channel as marketing tools.</p>
18. Would investors have increased confidence in financial reporting as a result of increased audit firm transparency?	Yes, as the audit firms' transparency improves audit quality, therefore, it should enhance investors' confidence in financial reporting.
19. Are there significant benefits to investors of increased audit firm transparency, since they invest in companies and not audit firms?	<p>The significant benefits of audit firms' transparency is that the transparency helps uplifting audit firms' standards, therefore, it helps improving audit quality and enhancing investors confident.</p> <p>The disclosures also give fundamental information to investors in their analysis of financial statements in order to make decisions on their investment.</p>
20. Should regulators consider areas outside of audit firms' governance, audit quality indicators,	Audit firms' governance, audit quality indicators (regarding ISQC1), and financial information should be enough, however, the regulator should closely monitor the reliability of disclosures as well as have

Questions	Comments
and financial statements for potential disclosures?	regularity inspections to ensure that audit firms follow their audit quality control policy and procedure that are in line with ISQC1 and ISA220.