



The Hundred Group
of Finance Directors

Investor Relations & Markets Committee

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Dear Hazel

APB – Revised draft ethical standards for auditors

We are pleased to submit our comments on the above proposals.

Who we are

The Hundred Group is a non political, not-for-profit organisation which represents the finance directors of the UK's largest companies, with membership drawn mainly from constituents of the FTSE100. Our aim is to contribute positively to the development of UK and International policy and practice on matters that affect our businesses, including taxation, financial reporting, corporate governance and capital market regulation.

Summary

The Hundred Group recognises that the debate surrounding Audit Partner rotation is critical, and that there is a balance that needs to be struck between Audit Partner independence and effectiveness. Whilst we note that the Ethical Standards consultation considers a range of points, our response only addresses this matter.

Our members are typically highly complex organisations and therefore in order for an Audit Partner to be effective – in other words experienced, knowledgeable, respected and able to bring to bear appropriate challenge – a longer period of service is required. The perceived risk that independence is compromised through a longer period of service is a lesser risk than that arising from an ineffective Audit Partner. The Hundred Group fully supports a seven year rotation period and sees little reason for a five year default position.

In our opinion:

- A five year cycle typically involves a one year learning and one year succession year, leaving only a three year “middle” period. Extending to seven years provides five “middle years”;
- The Audit Committee retains responsibility for reviewing the effectiveness of the Audit Firm and Audit Partner and can initiate a rotation at any stage within the rotation period;
- An experienced and knowledgeable Audit Partner understands an organisation and his/her judgment is respected within the organisation – it takes time to build up this trust and respect;

- Whilst a longer period could result in over-familiarity, this is compensated by a perceived lack of challenge from an inexperienced Audit Partner;
- The permitted service period of a Non-Executive is ten years, and during this period independence is not deemed to be compromised; and
- Moving to a seven year rotation would bring the UK rules in line with IFAC.

We set out in an Appendix to this letter our response to some, but not all, of the specific questions raised by this consultation.

Please feel free to contact me if you wish to discuss our comments on the proposals.

Yours sincerely

Peter Williams

The Hundred Group – Investor Relations & Markets Committee

Appendix 1 – Responses to consultation questions

Question 3: The APB would appreciate commentators' views on whether it would be appropriate to provide greater flexibility to ES 3 (Revised) to permit in certain circumstances, and with the prior approval of the audit committee, the rotation period to be extended from five to seven years.

As set out in the body of this letter, we believe that there is a strong case for moving to a seven year Audit Partner rotation period. We observe that the Audit Committee is already responsible for reviewing the effectiveness of the external Audit Firm and Audit Partner and has powers – either through removing the Partner or Firm – where it considers the facts warrant such action. In our opinion, this is a powerful right which preserves independence.

Additionally, the weight of audit regulation has changed since the APB last considered its position. We note the advent of the Audit Inspection Unit as well as a raft of Independence checks and procedures undertaken by Audit Firms.

We believe that together, these provide stakeholders with sufficient assurance that the Audit Partner is independent *and* effective.

Question 4: In addition to large listed companies which are also complex or diverse, are there any other circumstances where some flexibility as regards the rotation period for audit engagement partners on listed companies would be appropriate? If so, please explain the rationale for your views.

We believe that all Hundred Group members are complex or diverse, and find it difficult to see where the APB would draw the line. Indeed the complexities of smaller companies can often be more significant since the issues and judgments are likely to be more material to the enterprise.

In our opinion business is becoming more complex and therefore the risks attached with shorter rotation periods are far less significant than from inexperienced Audit Partners making ill-formed judgments.

Question 5: Do you agree that if an audit committee is able to decide to extend the period of rotation, this fact and the reasons for it should be disclosed to shareholders?

We agree in principle, but draw your attention to our other comments.

Question 6: Do you agree that the APB should retain the existing requirement and provide additional guidance in respect of partners and staff in senior positions for a continuous period longer than seven years?

The Hundred Group recognises the critical role that other auditors undertake in supporting the Key Audit Partner, and note that decisions regarding the continuing association of such individuals are not only challenged by the Audit Firm, but that the appropriateness of such a decision is also considered by the Audit Committee.