

27 May 2015

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## **AFME response to Consultation Paper PRA CP8/15**

Dear Pat

Please find attached the AFME response to CP 8/15.

Please do not hesitate to contact us if you would like to discuss the issues covered in this submission or would like us to provide further information about any of the matters which our members have raised. We would be happy to continue to engage with the PRA in ongoing dialogue on this and, in due course, may raise with you any further issues on the subject that AFME members bring to our attention.

Yours sincerely

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## AFME response to Consultation Paper PRA CP8/15

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The Association for Financial Markets in Europe (AFME) welcomes the opportunity to comment on PRA CP 8/15 on **“Engagement between external auditors and supervisors and commencing the PRA’s disciplinary powers over external auditors and actuaries”**.

AFME represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. We advocate stable, competitive, sustainable European financial markets that support economic growth and benefit society.

AFME is the European member of the Global Financial Markets Association (GFMA) a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association (ASIFMA) in Asia.

AFME is registered on the EU Transparency Register, registration number 65110063986-76.

We summarise below our high-level response to the consultation, which is followed by answers to the individual questions raised.

As the Consultation Paper does not raise direct questions on which the PRA seeks views, AFME offers its comments on matters which reflect the current thinking of its Members. Given the nature of the AFME membership we will focus those comments on aspects of the consultation paper that relate to the production of written reports by auditors, leaving any specific response in relation to disciplinary powers over auditors and actuaries to others more directly involved.

### Comments

AFME members feel that it is important to draw a distinction between the understandable desire of the PRA to utilise a standard set of questions (reviewed on an annual basis) to establish greater consistency in the areas of focus for all relevant firms, and the method by which that consistency is achieved.

In particular, members believe that it would be significantly more efficient and cost effective if the PRA were to provide relevant firms with the list of questions to be answered early in the year (for example in January or February) with firms being required to submit a full and final response back to the PRA within a set timeframe (say 150 – 180 days). The response to the questions raised by the PRA could then be prepared by the relevant firm making use of its Internal Audit and Compliance functions, rather than external auditors. The final response from the firm would be submitted to the PRA by the appropriate senior management (e.g. the CEO).

Clearly the wording of the specific questions to be answered would need to reflect the fact that a firm, rather than its external auditor, was being asked to provide the answers. AFME members do not believe that such a revised approach would significantly impair the ability of the PRA to establish appropriate content and consistency across the range of firms required to participate in the exercise.

Members believe that the following points are relevant:

- By adopting the approach suggested above, the greater consistency in areas of focus sought by PRA will be achieved in a timelier manner than would be the case were external auditors producing reports as a part of the annual statutory audit cycle. The PRA would, on the assumption that it published the list of questions by end February in any given year, have a full set of responses from the relevant firms by no later than end of August the same year (assuming firms were allowed six months to complete their reports).
- Adopting the approach set out in the CP would mean that the PRA would potentially have to wait until much longer for the reports to be completed so that, for example, with the list of questions being established by the end of February the statutory auditor for a firm with a December year-end would not be required to submit their report to the PRA until the end of April the following year, some 14 months after the PRA had established the set of questions to be answered in the report.
- By adopting the approach set out in the CP, AFME Members believe that the PRA are in effect outsourcing a significant element of their supervisory function to audit firms. It is clearly the responsibility of a regulated firm to explain the methodology it has used to assess risks, and the associated judgments and actions made by it to address the risks identified. Seeking to use the services of the external auditor to assess the efficacy and appropriateness of the risk assessments, assumptions made and judgments made by a firm goes significantly beyond the role of the auditor undertaking a statutory audit. Members believe that the effect of such an approach is to require the auditor to exercise judgments akin to those required of a supervisor/regulator.
- The use of firms' own staff to prepare and submit the response to the PRA would be significantly more cost-effective. AFME Members take their obligation to provide regulators including the PRA with accurate and comprehensive data in response to regulatory enquiries very seriously. Consequently members believe that it would not be unreasonable for the PRA to rely on firms rather than external auditors to provide answers in response to the specific questions raised by the PRA. PRA supervision staff can then make their own judgement as to the actions taken by the firm and decide whether or not they believe the firm to be in compliance with regulatory requirements. They can always commission a Skilled Persons Report under s. 166 FSMA if they have concerns.
- There is a genuine concern that, faced with the imminent prospect of the PRA applying disciplinary sanctions against auditors, audit firms may adopt an overly-cautious approach to assessing firms against the standard questions the PRA want answered. It would be unfortunate if the PRA proposals resulted in auditors (and consequently firms) taking an excessively risk-averse approach to matters in an attempt to avoid any form of criticism or financial penalty. It would, in effect, mean the whole exercise being time- and resource-costly, but not necessarily of value.
- In the unlikely event that a firm was found to have been careless in their approach to answering questions or deliberately misleading the PRA in any way, the firm would of course be liable to appropriate enforcement/disciplinary action by the PRA.
- Whilst not originating from the external auditor, the reports produced by individual firms could still be used to augment the bilateral and trilateral communications between the PRA, auditors and audit committees.

In view of the above AFME members request that the PRA redraft its proposals with regard to requiring written reports from auditors such that the required information can be provided directly by the relevant firm.

We would be pleased, of course, to discuss the issues covered in this response with the PRA or to provide further information if that would be helpful.

Responsible Executives

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