



BANK OF ENGLAND
PRUDENTIAL REGULATION
AUTHORITY

Rt Hon. Nicky Morgan MP
Chair, Treasury Committee

Rachel Reeves MP
Chair, Business, Energy and Industrial
Strategy Committee

Rt Hon Frank Field MP
Chair, Work and Pensions Committee

Sam Woods
Deputy Governor, Prudential Regulation,
CEO, Prudential Regulation Authority

16 July 2018

Dear Chairs —

Audit of Goldman Sachs

Thank you for your letter of 12 July 2018 on the above subject. As I explained during a hearing with the Treasury Committee on 11 July, the particular focus of a media story on a single bank and audit firm is in my view overstated. However, the issues you raise are important and I set out our approach below.

The PRA is not an audit regulator or inspector – that is the role of the FRC in the UK. Nevertheless, we have a significant interest in the quality of the audits of the firms we regulate, not least because our supervisory approach relies in some areas on high quality audit, and we gain value from productive dialogue between each audit team and the relevant supervisor. Given this, we: liaise closely with the FRC; discuss aspects of the audit in a range of bilateral, trilateral and roundtable discussions with regulated firms, audit firms and other regulators; and carry out various activities designed to encourage the delivery of improvements in audit quality.

In all of this work we seek to ensure that no audit firm has an advantage in the marketplace over any other as a result of our activity. So for example, as a general rule, even when the focus of our discussions and activities is on PRA-regulated firms audited by the Big Four audit firms, mid-tier audit firms that have in the past professed an interest in that market are invited to participate¹. Whilst we cannot compromise our focus on audit quality, our approach is indifferent to who the audit firm is and we see no reason why mid-tier audit firms cannot be considered suitable candidates to carry out audits of PRA-regulated firms.

As you note in your letter, the PRA is engaged in the process for appointing new auditors, particularly in light of the audit rotation rules. It is for the regulated firm to run the tender process and reach conclusions as to which audit firm they would like to appoint, but we are kept informed as things progress.² When we think it necessary we will discuss aspects of the process with the regulated firm or with one or more of the audit firms that are or might be tendering for the work. Sometimes those discussions come before the tender process has started – a recent example of that is the issue which gave rise to your letter, where a number of mid-tier audit firms have approached the PRA about the possibility of being engaged by a complex regulated firm. When approached in this way (and in answer to your question about skills, resources and experience) we seek to understand whether a high-quality audit can be delivered. We consider a number of aspects, which are based upon the observation that the ability to deliver a high quality audit becomes more challenging as the scale and complexity of a regulated firm increases. To understand this better, we are particularly interested in: the availability of appropriate skills and experience; adequacy and location of resources; and the existence of internal processes that help to

¹ Grant Thornton has participated in each of the 8 roundtable discussions I have held with auditors over the last two years.

² The PRA's rules require that before a PRA-regulated firm appoints an auditor it takes reasonable steps to ensure that the auditor has the required skill, resources and experience to perform its function, and PRA-regulated firms must take steps to ensure that an auditor provides information to the PRA in accordance with reasonable requests.

ensure audit quality (for example, review processes, engagement control processes, proper senior leadership oversight and so on).

Sometimes, an audit firm does not currently have the skills, resources and infrastructure to deliver an adequate audit, but plans to acquire them in advance of the appointment. Where that is the case it is important to look closely at the plans the audit firm has. Our expectation is that the regulated firm would consider all of this during the course of the tender process. When we are approached directly by an audit firm, we look for the audit firm to show us either that it already has the necessary skills, resources and experience, or that it has plans to acquire them without risks to audit quality.

Finally, I should say that I share the concern you express about an apparent lack of diversity and choice in the market for audit services for some of the firms we regulate. We do not have a complete view of concentration in audit markets, which seems more properly an issue for the CMA and/or FRC, but observe that larger regulated firms do sometimes seem to have a limited choice when they rotate their auditor, in much the same way as you describe in your letter.

I hope this provides you with the assurance you sought in your letter.

Yours sincerely,

A handwritten signature in black ink, appearing to read "S. Woods". The signature is fluid and cursive, with a long horizontal stroke at the end.

Sam Woods
Deputy Governor and CEO, Prudential Regulation Authority