Denis Kelly
Competition Commission
Victoria House
Southampton Row
London
WC1B 4AD

By e-mail: denis.kelly@cma.gsi.gov.uk

23 August 2014

Dear Mr Kelly,

Response to Competition and Markets Authority - The Statutory Audit Services for Large Companies Market Investigation: public consultation on the proposed Order

I am writing on behalf of the GC100 to respond to the above consultation. We submitted a response to the provisional findings and possible remedies in relation to this investigation on 20 March 2013 and to the notice of a further possible remedy on 19 June 2013 and to the Provisional Decision on Remedies on 15 August 2013.

GC100 is the association for the general counsel and company secretaries of companies in the UK FTSE 100. There are currently over 125 members of the group, representing some 81 companies.

Please note, as a matter of formality, that the views expressed in this letter do not necessarily reflect those of each and every individual member of the GC100 or their employing companies.

Thank you for giving us the opportunity to comment on the draft Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014 (draft Order).

We are pleased the Competition and Markets Authority (CMA) has been mindful of the new EU Directive and Regulation in preparing the draft Order. The EU Directive and Regulation are far-reaching and the CMA proposals must, in our view, be aligned and not inconsistent with these.

The UK Government has indicated its intention to consult later this year on implementing the EU Directive into national law. The implementation will require amendments to the Companies Act 2006, the UK Corporate Governance Code and potentially additional legislation. The Financial Reporting Council (FRC) is the UK's independent regulator responsible for promoting high quality corporate governance and reporting to foster investment. The FRC's remit already covers several of the areas within the draft Order, and it would be confusing and duplicative for the CMA to create a new set of rules which overlap and potentially conflict with existing and/or soon to be promulgated rules. We feel the CMA must be mindful not to create additional legislation and also not to distort the UK market by creating any differences between UK companies (in particular

more onerous provisions) when compared with their EU counterparts. The additional requirements, as currently drafted, are unnecessarily burdensome.

Accordingly, we have the following specific matters to raise:

1. We suggest that the wording on the Audit Committee's responsibilities is removed (section 5), as these are covered separately within the EU Directive and are already subject to existing guidance from the FRC, namely the FRC *Guidance on Audit Committees* (first published in 2003 and most recently updated in September 2012) and the FRC *Guidance on the use of audit firms from more than one network.* The wording in section 5 is confusing, in some case duplicative, and in others differs from existing guidance which is tried, tested and robust.

2. The prohibition contains two parts. Section 3.1a uses different wording for tendering and rotation when compared with the EU regulation. The draft Order refers specifically to a prohibition unless there has been a "competitive tender", while the EU regulation refers specifically to a prohibition unless there has been "auditor rotation". The draft Order does not add anything to existing law.

3. We have suggested some improvements to Section 3.1b, Section 5.1 and Section 5.3 by way of mark-up in Appendix 1. Please note that shareholders in general meeting will approve the appointment of the auditors (acting on the recommendation of the Board, through the Audit Committee) and authorise the Audit Committee to agree the auditor's remuneration.

   The Audit Committee should have responsibility for "Oversight" of the process and "Approval" of the engagement, but most Audit Committees will require management to run the tender process, given that Audit Committee members are independent non-executives, and do not "manage" the staff who actually runs the process. We have thus adjusted the wording to allow more flexibility.

4. The additional disclosure requirements in section 4.1, 4.2 and 4.3 are unnecessary for inclusion in this draft Order as the issues are adequately covered in the EU directive, which will be implemented into national law in due course. Furthermore, the obligations under 4.1 and 4.2 will, in our view, lead to boilerplate disclosure from year 5 onwards as many companies will have a base case disclosed of using the full 10 years until tender (and in many cases 20 years under rotation if UK law allows), unless and until a decision is made to the contrary.

Additionally, we feel that the draft order needs to consider the following items:

5. The prohibition does not currently allow for any exceptions. There may be certain situations (such as companies completing Class 1 transactions, mergers, companies entering the FTSE 350 for the first time) and other reasonable extenuating circumstances that should allow a tender to be postponed. The length of time it takes to plan and execute a tender – typically two to three years, in our experience - should also be taken into account. Section 3.1 should therefore include a new paragraph for such exceptions. Appendix 2 sets out some proposed areas to clarify and possible exceptions to consider.

6. There is improved clarity on the tender timetable but it would make sense to issue a table

or questions and answers showing at what point appointments have to be tendered under the Order, especially where first appointment was in the period from 2004 – 2006 (the problematic years under the EU Regulation).

7. The compliance statement seems to catch the 2014 reporting year (see 7.3) which seems odd when there is no obligation to tender yet. The requirement in section 7.3 is to state compliance with transitional audit tendering rules. It would be clearer to have compliance statements published in annual reports from when audit tendering is required.

Finally, we would take this opportunity to emphasise that many FTSE 100 companies use services from all four of the Big 4 accounting firms. In addition, mid-tier firms are often used for some services. To have any chance of making the market for audit services more competitive, the burden on tendering and independence rules needs to be kept to the minimum to minimise the cost to both auditors and the companies of changing suppliers, or using more than one supplier of accounting, audit and tax services.

We would be happy to discuss any of these points with you further.

Yours sincerely

Mary Mullally
Secretary, GC100
+44 (0)20 7542 7194

Appendix 1: revision to Audit Committee responsibilities

3.1 (b) the terms of the Statutory Audit Services Agreement, including, to the extent permissible by law and regulations, the Statutory Audit fee and the scope of the Statutory Audit, are approved between:

(i) the Audit Committee, either acting collectively or through its chairman, for and on behalf of the board of directors; and

(ii) the Auditor.

5.1 Only the Audit Committee, acting collectively or through its chairman, and for and on behalf of the board of directors, is permitted to:

(a) to the extent permissible by law and regulations, agree and approve the Statutory Audit fee and approve the Statutory Audit plan each year;

(b) initiate a Competitive Tender Process;

(c) make recommendations to the board of directors as to the Auditor Appointment decision pursuant to the Competitive Tender Process;

(d) recommend to the Board the appointment of the Audit Engagement Partner;

and

(e) subject to Article 5.2, and to the extent permitted by law and regulations, authorise an Auditor or Incumbent Auditor to provide any Non-Audit Services to the FTSE 350 Company or the Group of which that FTSE 350 Company is a part.

5.2 The Audit Committee may set a materiality threshold based on the value of the Non-Audit Service engagement below which the authorisation of the Audit Committee is not required.

5.3 The Audit Committee may consult such persons as it deems appropriate in the performance of the obligations in Articles [3.1(b)] [4.1] [5.1] and [5.2] and will typically engage extensively with management during the process. Typically management will run the tender and act as the liaison between the Audit Committee and the auditors.

Secretary: Mary Mullally - GC100 c/o Thomson Reuters Legal UK & Ireland, Friars House, 160 Blackfriars Road, London SE1 8EZ
T: 44 (0)20 7542 7194 - **E:** mary.mullally@thomsonreuters.com

Appendix 2: Additional exceptions or items to explain

We feel that there are certain exceptional circumstances under which companies should be allowed to defer their audit tender for up to two years. Under the draft Order, the following items are not currently considered:

a) Where there is a merger or class 1 transaction involving two companies of similar size, do the predecessor auditors of both companies need to be considered as the incumbent auditor?

b) In the case of a newly incorporated FTSE350 company following a corporate transaction (such as a merger or acquisition), can the company be treated as having no incumbent auditor?

c) Where a group of companies uses two or more external auditors, should the draft Order apply only to the auditor of the FTSE 350 company or should it also apply to auditors of all separate listed companies within the group, or all material group companies?

d) If there are structural changes in the audit market, for example the merger of two audit firms, then could a company be required to tender for a second time in ten years?

e) If a Senior Statutory Auditor were to move to a different firm, then could a company be required to tender for a second time in ten years?

f) In the instance of a Force Majeure, or a major incident impacting on the company (such as significant Going Concern risk and appointment of administrator, or a major disaster), we feel that an exception should be made. This is necessary because there are likely to be a number of advisors who would be conflicted from being independent for audit purposes and a tender could be detrimental to the company.

GC100 Group The Association of General Counsel and Company Secretaries of the FTSE 100
The GC100 Group is an unincorporated members' association administered by Thomson Reuters.
Secretary: Mary Mullally - GC100 c/o Thomson Reuters Legal UK & Ireland, Friars House, 160 Blackfriars Road, London SE1 8EZ
T: 44 (0)20 7542 7194 - **E:** mary.mullally@thomsonreuters.com