



Inquiry Manager
Statutory Audit Investigation
Competition Commission
Victoria House
Southampton Row
London
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By e-mail: auditors@cc.gsi.gov.uk

15 August 2013

Dear Ms Carstensen,

Response to Competition Commission – Statutory Audit Services Market Investigation – provisional decision on remedies

I am writing on behalf of GC100 to respond to the above provisional decision. 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.

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.

Our views are as follows:

Remedy 1: Mandatory tendering

We are opposed to the proposal that FTSE 350 companies should put their statutory audit engagement out to tender at least every five years, and that companies must go out to tender by the end of year seven.

As advised in our response to the provisional findings and possible remedies, we support the provision in the recently revised UK Corporate Governance Code that the external audit contract should be put out to tender at least every ten years on a comply or explain basis and believe that this new regime should be allowed time to take effect before any further changes are made. We note that a number of audit tenders have already been announced under the existing regime, which indicates that the new provision is already beginning to have an effect.

We believe that five years is too short, and that the ten year period is more supportable. Ten years reflects the work involved both for the company and for the auditor and prospective auditors in the tendering period. It also allows time to educate a new auditor about the company and properly gauge their performance levels before the cycle of tender preparation commences once again. The proposal could actually have the opposite effect to that intended in that it takes time for a new auditor to understand the full complexities of a new client, particularly in a widespread international group. This could lead to a lesser audit quality in the early years of an appointment.

GC100 Group

The Association of General Counsel and Company Secretaries of the FTSE 100

The GC100 Group is an unincorporated members' association administered by the Practical Law Company Limited

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More frequent change may result in less willingness to make an upfront investment into getting up to speed, and could ultimately result in a reduction in audit quality and higher costs.

Such short tendering intervals may also lead to audit committees adopting a risk-averse “box ticking” approach to tendering by concluding that the benefits for shareholders of retaining the incumbent audit firm outweigh the risks of selecting a new auditor. This approach could, therefore, conversely reinforce audit market share of the top firms rather than freeing up the market to mid-tier firms envisaged by this remedy.

We also believe that it is important that the “comply or explain” basis is retained as there could always be some intervening event that makes it inadvisable to tender the audit in year ten, for example when there is a new Chief Financial Officer, new Chairman of the Audit Committee or takeover activity.

We still do not understand how tendering the audit every ten years necessarily increases the likelihood of more mid-tier firms being appointed auditors to FTSE 350 companies. Increased barriers to entry from higher costs of entering into a market tend to restrict new entrants to a market so reducing the likelihood of the mid-tier firms being able to compete.

We further believe that mid-tier firms are put off tendering for FTSE 350 contracts because of the time and resources required both during the tendering process and immediately after appointment.

There is a significant and unnecessary cost to business of a tender every five years both for audit firms and for companies. Audit firms will need to recoup the costs of a tender over a shorter, 5 year period of tenure and companies will need to devote additional management time to a tender on a more frequent basis. These costs will ultimately be borne by shareholders.

Given the strong views of GC100 members, if the Competition Commission does finally decide that five years is appropriate, we would suggest that transitional arrangements be made for companies who, at the point that the Order comes into effect, have not tendered their audit services for more than 5 years. Without such arrangements there could be considerable disruption to the market, caused by the volume of companies tendering at the same time. This could also inhibit the ability for smaller firms to participate in many of the tenders given their smaller resources, so creating a new barrier to competition.

Remedy 2: Audit Quality Review team review

The proposal that the FRC should examine the quality of the audit of each FTSE350 company every 5 years and larger mid-tier firms on an annual basis will lead to greater cost for the FRC in terms of resource. This cost will need to be met by audit firms and ultimately companies as their clients. We question whether more frequent quality reviews will actually lead to improved audit quality.

Remedy 3: Auditor clauses in loan agreements

We would not object to the removal of “Big 4” clauses in loan documentation on a prospective basis, although, as noted in our previous response to the provisional findings and possible remedies, we do not see that this would necessarily make a significant difference as to whether or not a company will decide to appoint a mid-tier firm. The decision to appoint a mid-tier firm will depend on their ability to conduct an audit of the complexity and scope required.

Remedy 4: Enhanced shareholder engagement

We question the value of an advisory vote for shareholders and do not see it as necessary. Shareholders already have the right to raise questions on the audit and financial reporting at the AGM and this right is rarely exercised. An advisory vote adds nothing to the existing powers of shareholders to vote annually on auditor re-appointment. Further, we do not understand how an advisory vote serves to promote increased competition in the audit market.

Remedy 5: Strengthening the accountability of the External Auditor

Boards should decide whether and when to tender audit services. As noted in our March 2013 response to the provisional findings and possible remedies, shareholders appoint the members of the board and delegate to them authority for running the company in the long-term best interests of shareholders as a whole. This includes deciding whether and when to tender audit services. In turn, the board selects members of the Audit Committee, who are responsible for overseeing, among other things, the audit.

Further, we note that it is proposed that only the Audit Committee is permitted to negotiate and agree audit fees and the scope of audit work, initiate tender processes and make recommendations for appointment of auditors. Much of the detailed preliminary work will need to be undertaken by management acting on behalf of the Audit Committee and the Audit Committee should instead retain oversight, provide direction and have final responsibility for review decision-making. The suggestion that only the Audit Committee can commit on the audit process undermines the principle of joint and several liability of the Board. Any recommendation by the Audit Committee, like any other action of a Board Committee, must be subject to the approval of the whole Board which will almost certainly contain the Chief Executive Officer and Chief Financial Officer. This is quite apart from the impracticability of an Audit Committee operating independently of executive views on process, people and value for money aspects of an appointment.

Remedy 6: Extended reporting requirements

It is only very recently that Audit Committees have received reports from the FRC's audit quality review process that relate specifically to their audit. We feel that these recent changes should be given time to have an impact, particularly as until now, audit quality reports have been discussed only between the audit committee and the auditors. There will be period of readjustment for companies and investors as the impact of the public airing of these matters is absorbed.

We would welcome the opportunity to discuss these issues with you further.

Yours faithfully



Mary Mullally
Secretary, GC100
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