Grant Thornton

Our Ref SAM/MSD

For attention of the Inquiry Manager
Audit Market investigation
Competition Commission
Victoria House
Southampton Row
LONDON
WC1B 4AD

National Office

Grant Thornton UK LLP
Grant Thornton House
Melton Street
London NW1 2EP

T +44 (0)20 7383 5100
F +44 (0)20 7383 4715
DX 2100 EUSTON
www.grant-thornton.co.uk

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Dear Sirs

Investigation into the market for the supply of statutory audit services to large companies in the UK

Grant Thornton UK LLP (Grant Thornton) welcomes the opportunity to provide evidence, with respect to the supply of statutory audit services to large companies in the UK, to the Competition Commission (CC) in response to the CC's "Issues Statement".

As one of the leading UK audit firms, Grant Thornton has a particular viewpoint and interest in the debate regarding audit market competition and we are well placed to understand and articulate the competition issues that face audit firms outside of the largest four firms in the supply of audit services to large companies. As part of the wider debate, Grant Thornton has previously submitted its views to the House of Lords Economic Affairs select committee and to the Office of Fair Trading (OFT), in addition to submissions made by Grant Thornton International Limited (Grant Thornton International) to the European Commission in response to the Commission's concerns surrounding the structure of the large company audit market within a number of European Member States.

We set out below our views and evidence on the Issues Statement in the order in which it is structured.

1 Background and characteristics

1.1 As set out in our letter of 11 November 2011, we consider that there are features of the large company audit market which prevent, restrict or distort competition (competition issues).

1.2 We concur with the CC's summary regarding the background and primary characteristics of the large company audit market (as set out in paragraphs 6-10 of the CC's Issues Statement). In our view, the existence of these characteristics combine to prevent, restrict and distort competition in the large company audit market in the UK, such as to constitute an adverse effect on competition pursuant to Section 134(2) of the Enterprise Act 2002.

1.3 Whilst the existing market characteristics and barriers to entry and expansion have limited the ability of Grant Thornton to make headway amongst the FTSE 350, we consider that were those barriers to entry and expansion to be removed we have the attributes, quality, resources and incentive to seek to provide audit services to the majority of entities operating within the FTSE 350 (as explained further below).

Grant Thornton has the capability to audit the majority of the FTSE 350

1.4 The CC's Issues Statement indicates that it may be that only the four largest audit firms (Big-4) have the capabilities and resource to service public interest entities operating in the FTSE 350, and in particular that only the Big-4 have the international capability necessary to serve large clients with significant operations outside the UK[1]. Grant Thornton strongly disagrees with this proposition.

1.5 We consider that we have the attributes, capability and the resources (both in the UK and internationally) to audit the majority of the FTSE 350. In particular, we note the following regarding Grant Thornton's credentials:

(a) Grant Thornton has the necessary international capability to audit the large FTSE 350 companies. Grant Thornton is a member of Grant Thornton International, a network of accounting and audit firms present in more than 100 countries, including all of the major business hubs across the world; in aggregate member firms employ over 30,000 staff. Therefore whilst we do not dispute the point that international capability is important to audit large corporate firms, Grant Thornton and other auditing firms outside of the Big-4 have the necessary international capability to carry out such audits;

(b) Grant Thornton International is a coherent and integrated global network where members comply with international auditing standards. In particular it has developed a global electronic audit platform which is used by every member firm. Its global audit quality assurance process (GTAR) complies with ISQC 1, the quality standard issued by the International Auditing and Assurance Standards Board. GTAR was developed at a time when Grant Thornton International was one of 6 founding member networks of the

1 Issues Statement, paragraph 9(a).

Forum of Firms[2] (the other founding members being the Big 4 and BDO International) and when those founding members cooperated in order to develop global quality assurance programmes on a consistent basis;

(c) Grant Thornton has substantial resources located throughout the UK. In particular, it operates in 27 locations across the UK, with approximately 4,000 staff supporting 200 partners, and a well-resourced technical department. This level of resource, coupled with the international reach of the Grant Thornton International network, would allow us to provide audit services to most companies currently operating in the FTSE 350;

(d) The quality of Grant Thornton audits is comparable with the Big-4. Audit quality parameters which exist in the market, primarily reports issued by the Audit Inspection Unit (AIU), indicate that over a sustained period the audit quality of Grant Thornton is comparable to that of the four largest audit firms. Similarly Grant Thornton has a substantial internal quality function which is consistent with larger audit firms and has a depth of resource available to keep abreast of changes in regulations and standards relating to accounting and auditing requirements. Accordingly, quality differentials do not provide an explanation for Grant Thornton having a lack of share in the provision of audit services to FTSE 350 companies; and

(e) To the extent that auditing clients also require additional advisory services, Grant Thornton is able to provide a range of different services to auditing clients. In particular, Grant Thornton has significant resources for providing assurance, tax compliance and advisory, due diligence, business risk assurance, corporate finance, forensic and investigation services, recovery, reorganisation services and financial services advisory, amongst others. In the year ended December 2011 Grant Thornton provided non audit services to 36 FTSE 100 companies and 66 FTSE 350 companies, with a varying degree of fee level and complexity, mostly in providing various ad-hoc advisory work, demonstrating our credentials in providing a range of services to large corporate firms.

1.6 The following examples also demonstrate that Grant Thornton has the resources and capability to audit large FTSE 350 companies:

(a) Grant Thornton has been approved by the National Audit Office and Audit Commission to audit substantial publicly funded bodies such as Non-Department Public Bodies and local authorities;

(b) Grant Thornton has been appointed, with the agreement of the Financial Services Authority, to conduct s166 skilled persons reports in respect of companies in the regulated financial services sector, including 2 in the FTSE 100 and 2 in the FTSE 250[3]. S166 reports commonly involve providing

2 Formally established in 2002, the Forum of Firms is an association of international networks of accounting firms that perform transnational audits. Members of the Forum have committed to adhere to and promote the consistent application of high-quality audit practices worldwide, as detailed in the FOF Constitution (www.ifac.org/about-ifac/forum-firms).

3 Under s166 of FSMA, the FSA has the power to require a firm to appoint a Skilled Person to produce a report on specified matters. The Skilled Person must be independent to the firm. The FSA uses s166 appointments as both a supervisory tool and an enforcement tool.. The review might involve a

expert commentary upon governance and controls arrangements which skills are relevant to the audit of FTSE 350 companies;

(c) Grant Thornton currently acts for a number of companies that, while they are not FTSE 350 companies themselves, have similar features (eg substantial international operations, complex activities or significant scale). Examples are given in Appendix A; and

(d) Grant Thornton has experience of auditing FTSE 350 companies (it currently audits 5 FTSE 250 companies plus 150 subsidiaries across 27 countries of one of the largest FTSE 100 companies) and has an ambition to provide audit and non-audit services to a greater range of FTSE 350 companies.

1.7 As an illustration of the above points, in 2010 Grant Thornton audited a former FTSE 350 entity which was in the regulated financial services sector. The entity had suffered a significant adverse trading result, its former Big 4 audit firm was replaced and its accounts for previous years were restated. Our largest annual audit fee for this company was £1.5m. A 2009 survey of audit fees charged to FTSE 350 companies shows that audit fees ranged from £82,000 to £38.6m, with an average audit fee of £5.5m in the FTSE 100 and £766,000 in the FTSE 250[4]. Appendix B provides an analysis of FTSE 350 companies showing size of audit fee. This analysis shows there are many companies within the FTSE 350 (246 FTSE 350 companies have an audit fee of less than £1.5m) that require less resources to audit (ie a lower audit fee) than our illustrative audit and where there is no evidence that the activities are significantly more complex.

1.8 Based on the points set out above, we believe that Grant Thornton is well placed to service the majority of companies in the FTSE 350. Grant Thornton remains committed to increasing its presence in the large corporate audit market over time and already has the capabilities and scale to audit many significant multinational groups within the FTSE 350. The minority of companies that the firm does not currently have the capability to audit are ones where the scale of resources required would represent an unreasonably large portion of the firm's audit practice (for example we would consider carefully whether we should audit a single entity with a fee above £3m, when the next largest audit fee in our current client base is significantly lower) or substantial depth of highly specialised technical resources (for example as required by the dozen or so systemic banks and insurance companies). We acknowledge that it will take time for the firm to build capacity to service a meaningful number of companies in the FTSE 350. In our presentation to the OFT in August 2011, we provided an example illustrating that a net gain of 9 FTSE 250 audits and a further 9 consortia audit appointments in the FTSE 100 (for, say, 25% of the group audit) over a 3 year period is a realistic proposition for Grant Thornton.

review of past business for a specific business area or type of business (for example, pension transfers or small cap stocks), or it could focus on systems and controls, either generally or for specific areas. It is also possible that corporate governance arrangements may be covered by a review.

4 Financial Director, audit fees survey 2009 (www.financialdirector.co.uk)

1.9 However the existing characteristics of the market and, in particular, the barriers to entry and expansion that exist in the market (as set out in section 7) have prevented firms such as Grant Thornton from entering the FTSE 350 market in any meaningful way. We believe that a comprehensive package of regulatory stimulus is necessary to cause a change, since market forces and the very limited regulatory interventions that have occurred to date have failed to lead to change in the market, which has resulted in a range of adverse outcomes for customers (as set out in sections 3 to 6 below). Were such changes to take place, we believe that Grant Thornton is well positioned over time to challenge the market positions of the Big-4 in relation to the provision of audit services to FTSE 350 companies.

Investors are calling for change

1.10 The ultimate customer of auditors' services is the investor/shareholder and many voices from the investor community have commented that they would like to see greater competition in the large company audit market. We set out below examples of quotes from oral or written evidence provided by a range of investors, or investor representatives, to the House of Lords Economic Affairs Select Committee:

(a) Paul Lee, Hermes

"the major concern (for us) is the lack of competition, but particularly the lack of competition on audit quality. I think it was very clear from the evidence that was received from the Hundred Group that the only competition that they experience is on price and certainly that is all that we are aware of occurring in the market. Part of the problem is the invisibility of audit quality. We've all referred to problems with the audit report not providing useful information. That's just an example of the lack of information there is about audit quality. In the absence of that information it's no wonder that there's no competition on that topic."……."the argument about internationalism doesn't apply to many companies in the 250. There are certainly a number of companies in the FTSE 100 to which that argument does not apply. Admittedly, many are very multinational but not all are and it would be entirely possible for certain of them to be audited by a decidedly smaller, less international firm."[5]

(b) Robert Talbut, member of ABI investments committee

"while we may well accept that with some of the very largest, the most international, companies, that is a reasonable argument (that international reach is required), we don't believe that that, therefore, applies right the way down the size scale. The degree of concentration within, for instance, the 250 companies within the UK is broadly similar to the degree of mix within the 100 companies. Now, I think that there are many, many companies within the 250 where those arguments of extreme complexity and extreme internationalism of the business just does not apply at all. But it doesn't appear that the market is operating, even within those sub-100 companies, to introduce a greater degree of competition and choice."[2]

5 Pages 297-303, House of Lords select committee on economic affairs, Auditors: Market concentration and their role, Volume II evidence

(c) Iain Richards, Aviva

"within the markets, there are some very entrenched perceptions in audit committees that the Big 4 is what you need to go for. That is reinforced by the fact that investors and the markets prefer the Big 4. In the absence of any real insight into the audit, big is safe. So the market punishes people who don't go for the Big 4. The bankers take exactly the same approach. You may have seen there's been a debate around some of the clauses in debt instruments requiring the use of Big 4 firms. So there is a very persistent attitude throughout the market and through the players in this dynamic, all of whom tend to focus too much on the Big 4. So just tasking the Big 4 without changing other things isn't adequate. There needs to be a wider range of change. Audit committees need to be forced to be much more transparent and thoughtful in what they're doing, and the audit committee report does need to be beefed up." [2]

(d) Guy Jubb, Standard Life Investments

"while we believe strongly that the concentration of audit markets is fundamentally unhealthy and represents a systemic risk that has the potential to undermine confidence, it is not so much the competition issue but it is the lack of choice that is the area of particular concern to us. We made representations to the European Commission and others in 2009 asking them to address this particular issue with a sense of alacrity. But we have come to this position where we are no longer comfortable with relying on market forces to create the resolution to this. We do believe that there has to be some regulatory or governmental intervention. We have waited a decade, give or take, for market forces to make a change and the strength of the oligopoly is not making any progress." [2]

1.11 The Association of British Insurers (ABI) is an authoritative voice of UK institutional investors. In its written submission to the House of Lords Economic Affairs Committee, the ABI stated "We see no good reason why the total market for audit amongst market-traded/listed companies needs to be as concentrated as it is within this top tier of four firms".

1.12 The Financial Reporting Council (FRC) is the regulator which oversees audit inspections of firms that audit Full List entities. In its written submission to the House of Lords Economic Affairs Committee, the FRC stated "We believe that market perception is the main barrier to the expansion of non-Big Four firms into the audit market for large public interest entities. It is notable how few of the smaller fully listed companies use a non-Big Four auditor in comparison to AIM companies. There appears no other obvious explanation for the difference in concentration between these markets. Mid-tier firms may not have the resources to audit the very largest companies, but they are quite capable of auditing a far broader range of companies than is currently the case.".

1.13 We believe the above commentators share our view that competition in the market for auditing services to FTSE 350 companies is not working effectively. The

Hemscott Rankings guide published in August 2011 showed Big 4 penetration by number of the FTSE 100 at 99% and FTSE 250 at 95%. However, these rankings showed that for all Stock market companies, Grant Thornton's number of audits (260) was only marginally behind Ernst & Young (275) and not significantly behind the firm with the largest number of audits, KPMG (380). The next largest firm was BDO (173). The Hemscott rankings have shown Grant Thornton to be the leading audit firm on AIM for many years. The Hemscott rankings show that there are a significantly larger number of (ie more than four) well represented audit firms of Full List companies outside the FTSE 350 and AIM. We believe this is strong evidence that concentration of audits in the Big 4 is prevalent within the FTSE 350 and that is the segment of the market on which the CC could usefully focus.

2 Possible adverse outcomes

2.1 We believe that it is clear from the OFT's analysis, and from the points we set out in our letter of 11 November 2011, that there is limited competition in relation to the supply of audit services to FTSE 350 companies. In consequence, we believe that improved competition could be expected, as a matter of course, to bring a range of benefits to customers (i.e. companies and their shareholders).

2.2 For example, improvements in competition can be expected to (i) result in large companies having greater choice over the provider of audit services; (ii) lead to improvements in the quality and efficiency of conducting audits as greater competition should be expected to ensure that auditors continue to build audit quality over time; (iii) potentially result in lower prices if there are more competitive tenders for audit services; and (iv) reduce the systematic risk of competition being further adversely affected if one of the four largest auditors were to exit the market.

2.3 We comment below on each of the possible adverse effects which the Competition Commission have highlighted in their Issues Statement in addition to suggesting an additional possible adverse effect which we believe should be considered, namely that of choice of audit provider.

3 Suboptimal audit quality and levels of innovation

3.1 In a normal market a combination of pressure from customers, transparency in relation to the quality of services and the price paid for those services, and competition will be expected to lead to higher quality services and lower prices. Conversely in a market in which the company (who pay the auditor) and the ultimate customer (shareholders) have different requirements, such as the supply of audit services to the FTSE 350, neither is well placed to assess the quality of an audit, and crucially when there is a lack of effective competition there is a danger that audit quality will be suboptimal. This is because the normal factors that ensure quality is at the optimal level for customers are absent. In this regard, audit quality may be suboptimal in two ways (neither of which deliver an optimal outcome for consumers):

(a) too low quality; or

(b) too high quality (i.e. unnecessary gold-plating).

3.2 Notwithstanding the above observations from the investor community and a general acceptance from various other participants that the market for audit services in the FTSE 350 is overly concentrated, over a sustained period the audit market has only consolidated further and the client market has shifted noticeably in the size and make-up of FTSE companies. We note that while there has been much discussion regarding the role of the auditor and the vision for the future, there has been no stepped change in the work being carried out to meet what investors are asking for. In our view the audit process and its deliverables have not evolved significantly and audit quality remains an opaque measure with the result that the end user (the investor) is dissatisfied with the process. There appears to be no opportunity for others to influence this situation. Given the current characteristics of the market, a certain lack of innovation is to be expected (at least as regards the FTSE 350) as the spur to innovation through the competitive process is absent.

3.3 We consider that it is generally difficult to monitor auditor 'innovation' levels as a parameter of audit quality, not least because auditor innovation may be driven by a number of areas such as efficiency of performance or building client relationships, and may not correspond to achieving a better or more expansive opinion over the truth and fairness of the financial statements.

3.4 We consider it important to note here the differences between the definition of audit quality as applied by investors, audit regulators and by the company. For example, our experience is that companies may perceive high audit quality to mean, among others, responsiveness, auditor/director relationships, providing access to directors to a more extensive director network, depth of understanding of the business and the ability to give advice on other services at relatively short notice. While these are areas on which all audit firms compete, they tend to be areas which are more subjective and cannot be taken as "audit quality measures" independently. However since the delivery of these attributes are perceived by companies as important, audit firms may over deliver on the provision of these areas (for which over-delivery the company pays more for), resulting in sub-optimal audit service delivery, in that the service is over-specified and does not match the requirements of the ultimate customer, the investor. Put another way, the apparent lack of transparency about true audit quality and the inability of audit committees and shareholders to judge whether the level of service is what is required, may result in a tendency to "over deliver" on measures which are client serving rather than audit requirements.

3.5 In our view, increased competition may be expected to lead to improvements in the level of auditor innovation and efficiency of conducting audits over time, as audit firms become further required to respond to investor demands to differentiate their audit offering. For example, an audit firm might be more prepared to examine ways in which the results of the audit could be made more transparent to investors as well as to management and the audit committee.

4 Higher prices and costs

4.1 We consider that one would reasonably expect lower audit prices if there are more competitive tenders for audit services, due to the increased competition that this would bring. There is existing evidence that suggests that prices are higher in the current large corporate audit market than would be the case in a more competitive market. These include (and are referenced by the CC in their Issues Statement):

(a) the Oxera report titled "Competition and Choice in the UK audit market" examined how audit fees and concentration were inter-related. This found evidence that market concentration and the market share of a given auditor in a given sector/year both have a statistically significant and positive impact on audit fees;

(b) the OFT carried out an updated version of Oxera's analysis which is referred to in the OFT's reference decision. The OFT concluded that it found evidence in line with the Oxera report (i.e. that concentration resulted in higher audit fees); and

(c) the report by LSE Enterprise conducted for BDO also concluded that there was a direct link between concentration in the audit market and higher audit fees, specifically in relation to UK listed companies.

4.2 In addition to the above evidence, we make the following points which are relevant:

(a) the profit margins (evidenced by average profit per partner) of the Big 4 firms are significantly higher than that of the leading mid-tier audit firms (Grant Thornton profit per partner in 2011 was £342,000 while the Big 4 firms presented profits per partner of between £663,000 and £763,000 in their latest publicly available accounts). This is a further indicator that the Big-4 firms may be charging much higher prices in the large corporate audit market; and

(b) Grant Thornton was recently appointed as auditor to approximately 150 subsidiaries across 25 countries to a company in the higher reaches of the FTSE 100. This led to a reduction in audit costs for the UK subsidiaries from £490,000 to £310,00. (We do not have the information in respect of the cost differential of overseas audits fees although we believe the savings run to £100,000s and potentially higher.) The initial assessment from the company is that they believe the quality of the audit service has also risen. (We can provide additional analysis of this audit engagement if that were helpful.) This suggests that the Big 4 are able to charge higher prices because of their reputation and a perception of capability and international reach.

4.3 In order to conclude in this area we believe that the CC could usefully conduct further analysis to investigate whether prices are proportionately higher for FTSE 350 companies than for companies outside the FTSE 350, and whether the Big-4 are earning excessive profits. This analysis may include carrying out:

(a) its own price/concentration analysis. In this regard, Oxera is planning to explain to the CC what further work could be undertaken to supplement the analysis that it carried out in its 2006 report in order to make the analysis even more robust;

(b) an assessment of the profitability of the auditing services provided by the Big 4 in order to see whether they are earning excessive profits from auditing. The profitability of the Big-4 could also be compared with that of other auditors operating just below the FTSE 350, including Grant Thornton; and

(c) an econometric analysis of the relationship between price, frequency of tendering, and number of bidders which should include the impact of a non-Big 4 audit firm being part of the tender. Such analysis could also assess the pricing patterns after the year of tender to see whether prices rise quickly in subsequent years.

5 Less competition in non-auditing markets

5.1 In the year ended December 2011, Grant Thornton provided non-audit services to 36 FTSE 100 and 66 FTSE 250 companies (i.e. a significantly higher level of penetration than in relation to audit services) , with a varying degree of fee level and complexity. Typically these services covered: tax compliance or consulting, due diligence, corporate finance, restructuring, forensic investigations, business risk assurance or financial services advisory. We have the scope and ambition to increase the level of service provision to FTSE 100 and FTSE 250 companies over time.

5.2 The above analysis indicates that there are specific features associated with an audit which means that, whilst Grant Thornton is a viable choice for large FTSE 350 companies for non-audit services, it is not currently a realistic choice for most FTSE 350 firms in relation to audit. This is despite Grant Thornton having the attributes, quality, resources and incentive to provide audit services to FTSE 350 companies.

5.3 If the features adversely affecting competition in the large corporate audit market are addressed, the acceptance of Grant Thornton in relation to other non-audit services means that the CC can be confident that Grant Thornton will become an effective competitor in relation to audit. This is evidenced by the fact that many of the services which Grant Thornton currently provides to large corporate firms have similar requirements for technical knowledge and application across a range of jurisdictions, e.g. business risk assurance, due diligence, international tax advice, corporate finance. Business risk assurance and due diligence engagements commonly involve providing professional opinions and commentary upon aspects of governance, internal controls and financial reporting, and tax advice can encompass provision of reports in respect of taxation exposures and uncertainties, which areas of advice and opinions would be relevant to an audit.

5.4 As the provision of audit services provides a doorway to being instructed on non-audit services, should the barriers to audit be reduced, it will become easier for Grant Thornton and others to compete for non-audit work. In other words, whilst Grant Thornton provides more non-audit than audit services to FTSE 350 firms, its inability to attract audit work still limits its ability to compete for non-audit work.

5.5 The UK listed audit market currently follows the Ethics Standards issued by the Auditing Practices Board which build on the IFAC code of ethics and which stipulate various requirements regarding the provision of non-audit services by the auditor. These ethical rules prohibit the provision of certain non-audit services in addition to setting parameters over the size and type of fees which are able to be charged. In many cases non-audit services are able to be provided by the auditor if appropriate safeguards are applied and the audit committee gives agreement to the service provision.

5.6 Notwithstanding acting in accordance with the above regulations, for many companies the first choice provider of non-audit services is currently the incumbent auditor. Grant Thornton's research into corporate reporting within the FTSE 350 "A Changing Climate, Fresh Challenges Ahead" indicates that companies in the FTSE 350 incurred on average non-audit fees of 80% of their audit fees in the period from May 2010 to April 2011 and, of these, 73 companies paid more to their auditor for non-audit services than for audit services. The report also shows that only 10 companies did not use their auditor to provide any non-audit services during the period of review.

5.7 The use of the auditor to provide non-audit services is justified by many companies by the auditor's experience and knowledge of the company and, assuming safeguards are applied, is not in itself an issue. However this scenario results in an environment where it is very difficult for firms outside of the auditor to build relationships and raise their profile with the company – in many cases with non-audit work being allocated to the auditor without consideration of other firms. This environment, when combined with the high concentration levels that exist in the FTSE100 and FTSE250 audit market, also makes investment by other firms in providing non-audit services to FTSE 350 companies a less attractive proposition than it might otherwise be.

6 Auditor choice

6.1 The characteristics of the FTSE 350 audit market (as set out previously) result in companies being restricted in their choice of auditor, especially in certain 'specialist' sectors. Companies may be forced into choosing one or two audit firms owing to independence rules over the provision of non-audit services and due to the lack of experience inherent in other audit firms. Firms may also be reluctant to appoint an auditor that is auditing the accounts of key competitors in the market. Conflicts of interest (both legal and commercial) can therefore result in choice of auditor being extremely limited, which is not adequately captured by a comparison of the market shares of the Big-4. Lack of choice inevitably leads to higher costs for the company and, ultimately, investors.

6.2 In this regard, Oxera stated in its 2006 report that "According to the audit committee chairs survey, around one in eight FTSE 350 companies have two audit firms conflicted out as alternatives to their current auditor, leaving them only one [alternative among the Big Four] in the event of an audit tender. Oxera also found that around one in eight companies in the survey use all of the Big Four firms across

audit and non-audit services, potentially restricting their effective short-term choice of auditor to zero."[6]

6.3 The OFT also noted that concentration in the auditing of some specific industry sectors such as banking, mining, and utilities may be substantially higher, as not all of the big four auditors are present throughout such sectors;[7] For example, in the financial services sector, there are only three of the Big-4 firms providing auditing services to the large banks in the UK. The need for independence means that an audit firm could not audit a bank which acted as a supplier of financial services to that firm. Such rules potentially result in choice of auditor being even more limited. Oxera stated in its 2006 report that "on the question of choice, Oxera has found that a limited number of UK-listed companies, primarily in the financial services sector of the FTSE 100, have no effective choice of auditor in the short run.".[8]

6.4 The House of Lords select committee also found that "most witnesses believe that the dominance of the Big Four limits competition and choice in the audit market. Ethically, audit firms are unable to accept work which would place them in conflict with other work for the same or other clients."[9]

6.5 Additional restrictions on the choice of auditors available to companies may also arise from specific regulatory requirements. For example, multi-national companies choice may be restricted by regulation, such as the Sarbanes-Oxley Act of 2002 in the US, which limits the ability of public reporting companies to appoint as their auditors firms who supply them with certain types of non-audit services.[10] Further, audit firms may have internal policies that prohibit them from taking an audit appointment where a substantial proportion of the company's subsidiaries are audited by other firms.

6.6 Grant Thornton is aware anecdotally that companies which enter the FTSE 350 and that have a non-Big 4 auditor have a history of transitioning to a Big-4 auditor relatively soon after. This trend is likely to be due to the Board and audit committee being under considerable institutional pressure to appoint a Big-4 auditor despite the arguments which are put forward for the use of a Big-4 auditor not being displayed (e.g. a need for international reach beyond that of mid-tier firms, a complexity capability or non-audit services capability which is outside that of the mid-tier firms). This institutional bias creates a restriction/distortion of competition. We recommend that the CC investigates whether the above trend is significant in practice through the preparation of analysis in this area.

6 Paragraph 5.3.1 of the Oxera report "Competition and Choice in the UK Audit Market", 2006.

7 OFT Reference, paragraphs 1.5, 4.27, 5.51.

8 Page i, fourth bullet, of the Oxera report "Competition and Choice in the UK Audit Market", 2006.

9 Paragraph 26, "Auditors, market concentration and their role", volume 1, Select Committee on Economic Affairs, 2nd report of Session 2010-2011

10 OFT reference decision, paragraph 5.66.

Theories of harm

7 The audit market is highly concentrated and there are high barriers to entry with the result that the four largest firms have market power

7.1 Grant Thornton considers that the points set out below indicate that the large company audit market is not operating effectively.

7.2 The large company audit market is highly concentrated. In particular:

(a) at present 99 companies in the FTSE 100 are audited by just four audit firms, with the leading supplier of audit services having over 40% of the market share by number of audits. The OFT's reference decision confirms that the four largest audit firms accounted for 99% of audit fees paid by FTSE 100 companies and 98% of audit fees paid by FTSE 250 companies in 2010. The very limited presence of firms other than the four largest in auditing FTSE 350 companies demonstrates that those firms currently offer very limited, if any, competitive constraint to the Big-4. As mentioned above, we note that the situation is exacerbated in certain industries within the market where there are sometimes only two or three key players. Independence rules, conflicts, and regulations further limit choice, which means that the choice of auditor for many companies will be even more limited;

(b) the high level of concentration amongst the four largest providers of audit services to large companies in the UK has persisted for a significant period of time. The OFT provided evidence to show that concentration in the audit market has been consistently high over the last 10 years.[11] The OFT also noted that there have been relatively limited changes in the market shares of the Big-4 auditors over time, both for FTSE100 and FTSE250 clients, which points to competition being muted (i.e. there is little evidence of large-scale market share shifting amongst the Big-4 auditors as would be expected from intense rivalry). In addition, the FRC Fifth Progress Report on the implementation of the Market Participants Group recommendations stated that there was "little indication that concentration in the audit market is reducing or is likely to reduce in the near future".[12] This is unsurprising given the barriers to entry and expansion that exist in the market (as set out further below), and the fact that Grant Thornton and the other suppliers of audit services have been unable to break the stranglehold that the four largest suppliers of audit services have on the market. In this regard, the CC might ask to review the internal strategy papers of the Big-4 to determine the degree to which they perceive mid-tier firms to be a competitive threat in the supply of audit services.

7.3 There are high barriers to entry and expansion in the market, which have prevented Grant Thornton and the other suppliers of audit services from being able to break in to the FTSE 350 in any meaningful way. These include the following:

11 OFT Reference, figure 2.

12 Financial Reporting Council Fifth Progress Report on the implementation of the MPG recommendations, June 2010, page 6.

(a) The reputation of the four largest firms, due to their size and dominance in the market, and the low level of auditor switching (as mentioned further below), is such that it is particularly difficult for a smaller player or new entrant to the market to build market share or to build relationships with key management in large companies. Given that audits are characterised by a degree of asymmetric information (e.g. between the audit committee and Finance Director, and between the shareholders and the company), buyers often choose auditor on the basis of service level, reputation and brand.[13] This creates a vicious circle as the four largest firms conduct the vast majority of the audits of large firms in the UK, which reinforces their reputation, and results in them winning more business from FTSE 350 companies;

(b) restrictions over the appointment of auditors currently exist both in written form and, equally importantly, in unwritten form. The effect is that only prescribed firms may be appointed as auditor. In other cases lending agreements "pre-approve" firms from prescribed audit networks which, while not explicit restrictions, often have the same impact in practice. The above practice is also applicable in the case of companies aspiring to be public interest entities, where auditors outside of the largest four can be precluded from acting for them;

(c) the reputational barriers and restrictions over the choice of auditor are demonstrably not related to capability or quality of the audit firms involved, as supported by inspection reports issued by regulators, but are sweeping and often impenetrable barriers which reinforce concentration;

(d) there is an institutional bias in the large company audit market which favours the Big-4. In particular, there is a misplaced perception amongst Audit Committees that the Big-4 auditors possess a range of attributes (such as greater resources, an international network, greater experience, the ability to recruit higher calibre staff etc.) necessary for auditing large companies, which the other auditors do not (and cannot) possess. As a result, Audit Committees are generally unwilling to 'break the status quo' for fear of recrimination. This makes it extremely difficult for mid-tier firms to penetrate the FTSE 350 in any meaningful way even though, as set out above, we consider that we have the attributes, capability and the resources (both in the UK and internationally) to audit the majority of the FTSE 350;

(e) there is a misplaced perception amongst audit committees that the Big-4 are better placed than mid-tier firms to provide information on the latest developments in international accounting standards, and additional services related to audit standards, which disadvantages smaller firms; and

(f) the Big-4 have existing links with Finance Directors and audit committee chairmen (i.e. those selecting or influencing the selection of auditor), and are

13 Paragraph 5.30 of the OFT's reference decision.

therefore more likely to be appointed on the back of their existing relationships with FTSE 350 companies.

7.4 Grant Thornton notes that both the OFT and the House of Lords Select Committee on Economic Affairs' report[14] concluded that barriers to entry into the large company audit market were high.

7.5 There are very low levels of tendering and auditor switching. The OFT noted that "it has been concerned for some time that the supply of audit services to large companies in the UK has low levels of switching due to high switching costs and therefore competition in the market is restricted"[15]. The OFT concluded that there is little incentive for companies to switch auditor because:[16]

(a) the technical quality of an audit is difficult to discern, and as a result it is difficult for audit committees and Finance Directors to determine accurately whether one audit firm would produce a higher quality audit than another;[17] and

(b) it can be even more difficult for shareholders, the ultimate customers of audit, to assess the technical quality of audits given asymmetries in information and expertise.[18]

7.6 The lack of incentive for companies to switch auditor is exacerbated by what the OFT considers to be high switching costs.[19] In addition to concluding that companies faced material costs in switching auditors, and had little incentive to do so, the OFT found that levels of tendering were, in fact, particularly low.[20]

7.7 Grant Thornton's research into corporate reporting within the FTSE 350 "A Changing Climate, Fresh Challenges Ahead" indicated that in the period from May 2010 to April 2011, only five FTSE 350 companies changed auditor. A report by the Economics Affairs Committee entitled "Auditors: Market concentration and their role" also showed that a FTSE 100 auditor remains in place for 48 years on average, with a FTSE 250 auditor having an average tenure of 36 years. Further 70% of the FTSE 100 have not held a (formal) competitive tender for at least 15 years, providing no opportunity for other firms to illustrate their audit offering.

Such low levels of switching make it extremely difficult for Grant Thornton and other suppliers of audit services to destabilise the position of the four largest audit firms and grow market share, particularly when FTSE 350 audits are tendered infrequently.

7.8 The size of the largest four firms is such that they are perceived by large listed companies as having stronger resources and carrying levels of insurance which are far higher than those carried by other audit firms. Unlimited liability encourages

14 Auditors: market concentration and their role, 30 March 2011, pages 5-6, for example.

15 OFT Reference, paragraph 1.3.

16 OFT Reference, paragraph 5.9-5.29.

17 OFT Reference, paragraphs 5.10-5.11. The Oxera Report, pages 24-5 and 88.

18 OFT Reference, paragraph 5.12.

19 OFT Reference, paragraphs 5.14-5.17.

20 OFT Reference, paragraphs 5.18-5.29.

audit buyers wishing to protect against falls in the value of their investment to appoint auditors with the greatest resources to satisfy a claim for deficient auditing.

7.9 Most Audit Committees of large corporate entities are unwilling to appoint an audit firm outside of the largest four for fear of criticism by investors and analysts. Whilst this fear may be unfounded it remains a powerful disincentive and most companies in the market are reluctant to change the status quo.

7.10 In our experience the reputational bias towards the Big-4 is particularly prevalent in unwritten form, with bankers and other advisors recommending, or in some cases requiring, that a particular audit firm should be appointed. A broad range of Grant Thornton partners encounter restrictions, primarily from a range of lenders and private equity houses, but we do not track those cases centrally. Grant Thornton International has obtained evidence of restrictive covenants with our member firms in the UK, Finland, Germany, Ireland and Spain possessing written evidence of restrictions. In the US Grant Thornton International has identified that at least 10% of the Russell 2000 companies are subject to some form of restriction on appointment of auditor or accounting adviser. The US is one of the few jurisdictions which require documents such as lending agreements to be placed in the public domain, via the EDGAR database. The informational asymmetry as between the Audit Committee and the Board and between the shareholders and the company also make the appointment of a Big-4 auditor a lower risk in terms of reputational association. Grant Thornton has been approached by the Finance Directors of existing clients who have informed us that banks have suggested that they would require a Big 4 auditor if the company sought to increase its bank facilities (We can provide additional analysis of some of these situations if that were helpful.).

7.11 The combination of the factors set out above make it very difficult for mid-tier firms, including Grant Thornton, to penetrate the FTSE 350 audit market in any meaningful way.

8 The four largest firms could bundle together services in order to create barriers to entry in the market for statutory audit and in related markets

8.1 We believe there is a misunderstanding by many companies regarding the application of ISA 600 "Special considerations – audits of group financial statements (including the work of component auditors)" with companies being misinformed that the ISA "requires" the use of the same auditor for all companies within a group. The misrepresentation of the auditing standard allows the incumbent auditor to bundle together the provision of statutory audit services to all companies in a large, often international, group and thus raises a barrier to entry for a secondary auditor to pursue the statutory audit service for subsidiary companies. The ability to appoint a different auditor to a subsidiary company would provide a low cost way of a company to quality test an auditor outside the Big Four and for that auditor to develop recognition and knowledge of the business.

8.2 We note that this bundling of audit services for the parent company and its subsidiaries is commonplace in the audit market, often based on the belief that having the services "packaged" provides a more efficient and cost-effective audit offering and the misconception that such an arrangement is required by ISA 600.

Grant Thornton has evidence of providing audit services to a number of subsidiary companies of a large multinational FTSE 100 business, while the audit of the parent company and other subsidiaries has remained with the Big 4 group auditor, which has allowed substantial cost savings over using a Big-4 auditor for 100% of the group audit. This saving has been achieved without a loss of audit quality as perceived by the company. This is further discussed in paragraph 4.2(b).

9 Customer conduct limits competition, in particular by tendering infrequently

9.1 As noted previously, the level of tendering in the large corporate audit market is very low. It is evident that rare tendering opportunities create a lack of competition and, moreover, a tender that remains limited to the Big-4 does not provide real competition within the market.

9.2 As mentioned above, there remains a restrictive reputational bias shown by companies and audit committees and companies primarily to consider audit firms within the Big-4. This reluctance is driven by informational asymmetries with companies and shareholders desiring different outcomes from the audit process and, with difficulty in the assessment of audit quality, most opt for the "safe" option of making a choice on the basis of reputation.

9.3 We believe that more frequent tendering, and particularly where auditors outside the Big-4 are invited to participate, is likely to lead to a fall in audit fees (particularly if the reputational bias towards the Big 4 is overcome). We recommend that the CC tests empirically during its investigative process whether the participation of auditors from outside the Big 4 in the tender process for FTSE 350 firms results in lower audit fees being charged.

9.4 In recent years Grant Thornton has submitted audit tenders for 3 FTSE 350 group audits, none of which has been successful in securing the audit. While the result of each tender will be decided by the audit committee based upon a range of factors, including price, two areas which are referred to when identifying reasons for an unsuccessful tender is the relationship which the audit firm has with key decision makers in the group and the understanding of the organisation, it is clear that these areas afford the incumbent auditor an advantage in the tender process.

9.5 As noted above in the section on non-audit services, the customer conduct of choosing the incumbent auditor for a significant proportion of non-audit services also limits the ability of firms outside of the Big-4 to compete.

9.6 We consider that very few exponents of audit would argue that an audit firm does not lose at least the perception of objectivity at some point where the relationship with a company extends over several decades. Whilst it is difficult to identify precisely when this point is – a number of commentators argue this is before an auditor has been in office for 48 years (the average in the FTSE 100).

9.7 An argument put forward by some commentators, including many of the Big-4 audit firms, is that tendering creates unnecessary cost, a fall in audit quality and a loss of auditor knowledge. However we consider that on an appropriate timescale, the cost of changing auditor is unlikely to be unpalatably restrictive to large companies (and

their investors), and the competitive process of more regular tendering could lead to lower audit fees. We note further that there is no compelling evidence that we have seen which proves that audit quality falls upon a change in auditor. In our view and experience there is a compensating benefit that the new auditor may unearth issues previously unnoticed by the incumbent auditor.

9.8 It might be helpful for the CC to elicit the views of the NAO, Audit Commission and Audit Scotland about the impact of a change in auditor on audit quality, since they will have monitored the audit quality of many entities where such a change has occurred.

9.9 The company's directors should be acting in the investors' interests and not looking at the audit service purely as a cost to the company. A perceived increase in costs due to more frequent tendering should not preclude the company from doing so, particularly if there is a genuine concern (or perception) that too cosy an auditor relationship could lead to business failures or declining audit quality (and lack of confidence in the capital markets).

9.10 We recommend that the CC considers performing its own further analysis to investigate the points made above to consider if there is any evidence of falling audit quality or restrictive cost implications of changing auditor.

10 Specific features of the market may make it particularly prone to risks of regulatory failures which could lead to a reduction or distortion of competition in the market

10.1 We have seen no evidence that there are regulatory failures which could lead to a reduction or distortion in competition in the market.

10.2 However, we believe that audit regulators in several leading countries are concerned about the possibility of another Big 4 audit firm failure following the collapse of Arthur Andersen. For example, in 2009 the FRC highlighted the forced exit of a large audit firm from the market as one of the major risks to the capital markets.

11 Tacit coordination between the four largest firms results in less competition in certain sectors

11.1 Grant Thornton is not in a position to determine whether tacit coordination has actually taken place amongst the four largest providers of audit services in the UK and we have not observed such behaviour. For the reasons set out below, we consider that all the conditions set out in the legal precedent, necessary to facilitate tacit coordination, are, however, present in the market for the supply of audit services to FTSE 350 companies.

11.2 The CC's market investigation guidelines ("CC Guidelines"), set out the following three conditions which are necessary for firms to be able to engage in tacit coordination:

(a) "First, the market has to be sufficiently concentrated for firms to be aware of the behaviour of their competitors, and for any significant deviation from the prevailing behaviour by a firm to be observed by other firms in the market";

(b) "Second, it must be clear that it will be costly for firms to deviate from the prevailing behaviour; so costly that it will be in the firm's interest to go along with the prevailing behaviour rather than seek to deviate from it"; and

(c) "Third, this type of parallelism can only be sustained in markets where there are relatively weak competitive constraints. If barriers to entry are low, then the threat of entry will tend to undermine such conduct".

Condition 1

11.3 The first condition is that the market has to be sufficiently concentrated for firms to be aware of the behaviour of their competitors, and for any significant deviation from the prevailing behaviour by a firm to be observed by other firms in the market. In relation to this condition, Grant Thornton considers that the following characteristics are relevant:

(a) the market is highly concentrated, which makes it easier for firms to monitor the behaviour of their competitors. The OFT presented much evidence to show the high levels of concentration in its reference decision. In addition, independence rules, conflicts, and regulations further limit choice and thus further increase market concentration;

(b) the market has remained highly concentrated for a significant period of time (as set out in section 7 above), which would enable coordination to be sustained; and

(c) there is market transparency amongst the Big-4 auditors, which allows them to observe and monitor the behaviour of their rivals.

11.4 In the above regard, the following points are relevant:

(a) First, as pointed out by the CC in the Issues Statement, the name of a company's auditor, is publicly disclosed in a company's annual report and accounts. This means that it is very easy to determine, at any point in time, which firm is the auditor for every FTSE 350 company and also to identify any changes in the status quo;

(b) Second, the audit fees paid are also publicly disclosed in a company's annual report and accounts. This means that the fees charged by rival auditors is highly visible, can be readily compared with the fees charged by rivals, and it would be very easy to observe if one of the Big-4 auditors is aggressively engaging in price cuts. It is not clear therefore why the CC states in paragraph 49 of the Issues Statement that tacit coordination on prices is less likely than collusion with regards to geography or industry sector;

(c) Third, as mentioned above, not all of the Big-4 auditors are present across all sectors which means that in certain sectors/industries there are even fewer rivals to monitor;

(d) Fourth, given that audits are subject to specific minimum standards, there is a high degree of transparency with regard to the audit services provided. Confidential and unique know-how and intellectual property is not a feature of this market to the extent that firms cannot gain an insight into the way their competitors execute their services; and

(e) There is stability in the demand for audit services (due to the fact that it is a statutory requirement for medium and large companies to have their financial statements audited externally under the Companies Act 2006), which makes it easier for the Big-4 auditors to decipher the actions of their rivals from random market-wide factors affecting demand. In this regard, it is of note that the OFT did not receive any responses to its consultation process that suggested that audit services had any substitutes.[21] Grant Thornton submits that the UK Audit Market is unlikely to experience any significant unpredictable market-wide changes in demand which might make it more difficult for the Big-4 to decipher whether a change in market share, for instance, is due to the actions of another firm or due to demand changes in the market as a whole. Accordingly, the stability of the demand for audits is a feature of the market which makes it easier for the Big-4 auditors to monitor the actions of their rivals.

Condition 2

11.5 The second condition necessary to facilitate tacit coordination is that it must be costly for firms to deviate from the prevailing coordinated behaviour. In this regard, Grant Thornton considers that the following characteristics of the audit market are relevant:

(a) First, it is easy for the Big-4 auditors to retaliate to the behaviour of rivals that deviate from a common policy by engaging in aggressive price cuts in the audit market or in the markets for non-audit services. As mentioned above, as the name of the auditor and audit fees are publicly disclosed in a company's annual report and accounts, the fees charged by rival auditors is highly visible. In addition, due to the commercial interaction amongst the Big-4 auditors in relation to the provision of both audit and non-audit services, retaliation to any deviation from a common policy in the audit market could also take place in relation to the provision of non-audit services. In other words, the multimarket contact of the Big-4 auditors in relation to the provision of both audit and non-audit services means that an aggressive price response could also take place in a different, but closely related, market. Grant Thornton would urge the CC to investigate whether such retaliatory behaviour has taken place (e.g. by analysing the internal documents of the Big-4);

(b) Second, an aggressive price response from rivals in response to any deviation from a coordinated outcome in the UK large company audit market would have a large detrimental impact on revenue and profitability This is for the following reasons:

21 OFT Reference, paragraph 4.18.

(i) Due the statutory requirement that large firms must be audited, any price cutting by the Big-4 auditors will have a direct impact on the total market revenue available from auditing. This is because the lower prices will not create any volume benefits in terms of a market expanding effect as all the large firms are already audited (i.e. the same level of audits will still be undertaken, just at lower prices); and

(ii) As the costs to the Big-4 of providing auditing services are largely fixed in the short term (e.g. in relation to staffing, management, and centralised costs), a reduction in revenue is likely to have a significant and immediate impact on profitability.

(c) Third, there is a clear profit incentive from engaging in tacit coordination compared to a competitive market outcome. As mentioned in the CC's issues statement, given that audits are a statutory requirement for large firms, the overall market demand for audits is likely to be price inelastic. This is because if audit fees increased, large firms would still have to purchase auditing services as there are no substitute products for an audit.[22] This means that auditing firms can earn higher fees and margins as a result of engaging in tacit coordination than they could from intense competition. This creates a clear incentive for the Big-4 firms to engage in tacit coordination, and for the coordination to be sustained, particularly in light of the large disciplining effects set out above.

11.6 The CC may wish to gather evidence on the bidding behaviour of the Big-4 when participating in tenders to audit FTSE 350 firms, and the extent to which Big-4 firms approach FTSE 350 firms directly to encourage them to switch or to run a tender.

Condition 3

11.7 The third condition necessary to facilitate tacit coordination is that the reaction of current and future competitors, as well as of customers, must not jeopardise that coordination. In other words, current and future competitors should not have the ability to destabilise any coordinated behaviour (e.g. by being able to expand and gain market share quickly).

11.8 Grant Thornton considers that the CC already has considerable evidence that existing market conditions are such that condition 3 is met. Specifically:

(a) As set out in section 7 above, there are significant barriers to entry and expansion in the audit market, which means that it is difficult for rivals to enter and destabilise any coordinated behaviour amongst the Big-4 auditors;

(b) there is very limited existing competitive constraint by mid-tier firms. Grant Thornton and the other mid-tier suppliers of audit services have been unable to break the stranglehold that the four largest suppliers of audit services have on the market; and

22 Issues Statement, paragraph 18.

(c) there are perceived switching costs which reduce the ability of rival auditors to gain market share and thus destabilise any coordinated behaviour.

11.9 We would encourage the CC to test for tacit coordination empirically for example by looking at the patterns of bidding behaviour to see whether there is any material difference in the price of bids when just the Big-4 auditors are involved compared to bids when non-Big-4 firms are also involved. It would also be worth looking at whether there is any material difference in the behaviour of the Big-4 when a firm from outside the Big-4 is the existing auditor of the FTSE 350 company, and comparing this behaviour to situations where other members of the Big-4 are the existing auditors.

12 Information asymmetries and conflicts of interest adversely affect audit quality and allow the four largest firms to maintain market power

12.1 In practice there are a number of information asymmetries regarding the audit process with conflict in particular between the desires of the ultimate customer (the shareholder) and the company. These have been noted further above in the sections on market characteristics and on audit quality.

12.2 We note that shareholders rarely have a role or understanding over the appointment or re-election of the auditor as, in practice, they are provided with only a binary choice at the AGM. The fact that many investors are calling for a change to the structure of the audit market, provides a clear signal that there is insufficient transparency over the process by which auditors are appointed, which further creates restrictions over the ability of an auditor to compete absent changes to the buying patterns of the audit committee.

13 The failure and exit of one of the four largest firms

13.1 There are certain markets, typically characterised by high concentration and high barriers to entry and expansion, where substantial negative effects could arise from the failure of a large supplier. This is especially likely to occur where business continuity (in terms of the service of that supplier) is essential to the on-going viability of other companies, and where there are a limited number of players willing and/or able to provide such business continuity. A related factor is the difficulty faced by new entrants in gaining the trust of businesses, and the importance (perhaps the necessity) of the supplier's reputation to those businesses. In such markets, the failure of a single firm can potentially lead to further business failure or damage to the confidence of the capital markets. There can be clear benefits from allowing the failing firm to be taken over, and from swift procedures to allow this to happen. However, in many cases, the firms that are best placed to provide effective business continuity will be the other major firms in the market. As such, there is a potential tension between ensuring stability and preventing further concentration in the market. For example, following the collapse of Andersen while a number of US partners of the former Andersen firm were admitted as partners to Grant Thornton LLP in the US, in most jurisdictions former Andersen partners substantially joined other Big 4 firms (for example Deloitte in the UK).

13.2 A 4-to-3 scenario may not have an impact on competition in the current audit market, but a failure of a Big-4 audit firm could have a detrimental impact on and cost to investors and the capital markets. High concentration increases the risk of a large audit firm failure having a detrimental impact on the capital markets, since the Big-4 currently audit most of the large companies in the FTSE 100 and thus more entities would be impacted by a failure.

13.3 Grant Thornton is enthusiastic to continue to contribute to the development of policies to enhance competition in the large corporate audit market and to address audit market structure and we would be pleased to have further dialogue with you to explore the comments made in this letter.

If you have any questions on this response, please contact either Steve Maslin (Direct T: +44 (0)20 7728 2736; E: steve.maslin@uk.gt.com) or Martin Drew (Direct T: +44 (0)1865 799914; E: martin.s.drew@uk.gt.com).

Yours faithfully

Grant Thornton UK LLP

Appendix A : Entities serviced by Grant Thornton which have features similar to many FTSE 350 companies

FTSE 350 companies can be typically characterised through their size, international reach and, as a result, the more complex nature of their operations. Set out below is a sample of Grant Thornton clients which have characteristics akin to a number of FTSE 350 companies and demonstrate that Grant Thornton currently has the credentials and capabilities to provide audit and non-audit services to these types of client.

Entities in italics indicate audit clients

Company	**Characteristics**
Sportingbet plc	Significant online gaming operator with over 2 million customers in 30 markets worldwide. Turnover of £200m+.
Atos Origin UK Ltd	An international information technology services company with annual revenues of EUR 8.7 billion and 78,500 employees. Serving a global client base.
KPMG LLP	A leading provider of professional services including audit, tax and advisory. Turnover of £1.6bn with 11,000 staff operating out of 22 locations.
Sabre Holdings Corp	A global travel technology company serving the world's largest industry, travel and tourism.
Japan Tobacco International B.V.	International Tobacco business, with employees in 60 countries generating $10.2bn sales worldwide.
Deloitte LLP	A leading provider of professional services including audit, tax and advisory. Turnover of £2.1bn with 13,000 staff.
Mears Group plc	Provider of care and social housing to hundreds of thousands of customers in the UK. Currently employing around 13,000 people with revenues of £525m.
Verizon UK Ltd	Leading provider of global IT, security, and communication solutions, with one of the world's most connected IP networks.
Cattles plc	A financial services group operating in the UK financial services markets of non-standard consumer credit and debt recovery. Revenues of > £500m and significant complex financial instruments.
Bank of America	One of the world's largest financial institutions with over 7 million credit card accounts in the UK, employing 4,000 UK staff.

Company	**Characteristics**
Jefferies International Ltd	A global securities and investment banking group, offers leading investment banking services to U.K. and European companies.
Iceland Foods Limited	One of Britain's fastest-growing and most innovative retailers. Employing 22,000 staff and with revenues of > £2bn.
Helical Bar plc	A property development and investment company holding assets of approximately £540m. A former member of the FTSE 350.
Olympic Delivery Authority	The public body responsible for developing and building the new venues and infrastructure for the Games and their use after 2012.
Nyrstar NV	An integrated mining and metals business, with market leading positions in zinc and lead, turning over €2.7bn worldwide.
Mott MacDonald Group Ltd	A management, engineering and development consultancy serving the public and private sector around the world. The group has 14,000 staff operating in 50 countries worldwide and has turnover of approximately £1bn.
Omnicom Europe Limited	A leading global advertising and marketing communications services company providing services to 5,000 customers in more than 100 countries and generating revenue of $12.5bn.
Norbert Dentressangle UK Ltd	A major European transport, logistics, and freight forwarding company. The company operates from 500 sites in 20 European countries and employs 26,000 people.
Matalan Ltd	One of the UK's leading clothing and homewares retailers, with over 190 stores in the UK.
Deutsche Bank AG	A leading global investment bank with 100,000 employees in 74 countries.
BUPA	A leading international expatriate health insurer with customers in over 190 countries and revenues of £7.6bn.
LCH Clearnet Ltd	A leading independent clearing house group, serving major international exchanges and platforms and assets of more than £500bn.
Torex Retail	A European market leader for store systems in Retail, Hospitality, Convenience and Fuel markets. The company employs 1,150 people and serves 6,000 businesses customers every year, in over 30 countries.

Appendix B : Analysis of FTSE 350 companies by market capitalisation showing audit fee

The graph below sets out an analysis of the audit fee paid by FTSE 350 companies (with reference to their most recent publicly available financial statements), for those companies with an audit fee of £5m or greater – representing 309 companies, compared against the market capitalisation of each company.