

## STATUTORY AUDIT SERVICES MARKET INVESTIGATION

### Note of call with Legal and General Investment Management on 23 May 2013

#### Background

1. The call was arranged at the request of Legal and General Investment Management (LGIM) to discuss its submission to the Competition Commission (CC). [REDACTED]. The LGIM Corporate Governance Team is independent of the company's active equity managers.

#### Summary of the discussion

2. LGIM set the context of why large shareholders, such as LGIM, had not been more proactive in challenging companies in the past, noting the need to gather a critical mass of votes, in the order of 15 per cent of votes to make a significant impact. As an example of issues for shareholders of raising concern, LGIM noted the recent voting at the JPMorgan Annual General Meeting where 32 per cent of voting shareholders had supported splitting the role of Chairman and CEO (and in 2012 it had been 40 per cent), which LGIM believed indicated significant shareholder concern, whereas in certain press it was interpreted as widespread support for maintaining the status quo.
3. Specifically on issues of audit, LGIM felt that the specialist nature of audit meant that it was something that investors did not necessarily feel able to engage with and was a very nuanced area of corporate governance and compared this to executive remuneration, which investors were much more easily able to engage with and understand.
4. LGIM had spoken to a number of Chairmen, Audit Committee Chairmen and non-executive directors about audit issues and steps that would be necessary to reform the market. It gave two specific examples of individuals it had spoken to. One was a non-executive director and Audit Committee (AC) member ([REDACTED]) of a FTSE 100 company ([REDACTED]), the other was a Chairman ([REDACTED]) of another FTSE 100 company ([REDACTED]). Both individuals had expressed sympathy for LGIM's suggestion of a 15-year mandatory rotation of audit firms.
5. LGIM's view was that 15-year mandatory rotation was not too draconian and was manageable especially compared with current EU proposals.
6. LGIM had adopted a voting policy in line with its submission to the CC, and so, over a suitable transition period, would vote against the reappointment of AC members as directors if a company did not follow what LGIM saw as best practice (ie holding tenders, changing auditor periodically, transparency and limiting the level of non-audit services (NAS)). Equally, LGIM would vote in AGMs against auditor reappointment if the audit had not been tendered in ten years, and if a company proposed to reappoint an auditor that had been in place for more than 15 years without sufficient explanation. LGIM believed that co-signatories of USS's submissions were likely to adopt a similar practice.<sup>1</sup>

---

<sup>1</sup> [www.competition-commission.org.uk/assets/competitioncommission/docs/2011/statutory-audit-services/uss\\_and\\_other\\_investors\\_pfs\\_and\\_remedies.pdf](http://www.competition-commission.org.uk/assets/competitioncommission/docs/2011/statutory-audit-services/uss_and_other_investors_pfs_and_remedies.pdf).

7. LGIM supported a cap on NAS provided by the auditor, as it felt that it increased the threat to an auditor's independence (and hence to audit quality), and that such perceptions were important to the investor. LGIM also saw particular benefit of spreading NAS contracts more widely, as it gave companies a better understanding of the services that firms could provide and would increase choice by increasing familiarity.
8. On AC reporting, LGIM gave cautious support for the changes to the Financial Reporting Council's Guidance on Audit Committees but thought it necessary to see what disclosures companies ultimately made before passing judgement.