Inquiry Manager
Statutory Audit Investigation
Competition Commission
Victoria House
Southampton Row
LONDON
WC1B 4AD

19 June 2013

Dear Sir/Madam

STATUTORY AUDIT SERVICES MARKET INVESTIGATION
Notice of a Further Possible Remedy under Rule 11 of the Competition Commission's Rules of Procedure

You have invited comment on

(a) the specification, effectiveness and proportionality of this remedy and, in particular, on the following: *(a)* whether giving the FRC a secondary duty to promote competition between audit firms will assist companies in comparing auditors; and *(b)* whether giving the FRC a secondary duty to promote competition between audit firms will assist shareholders to influence the auditor appointment decisions of companies in which they hold shares.

The Notice also states:

> *We consider that one effect of giving the FRC a secondary duty to carry out its functions, where appropriate, in a manner which it considers will promote competition between audit firms in the provision of statutory audit services to large companies, would be to require the FRC to consider how it might review and report on audits of large companies in a way which promoted competition.*
>
> *In our view this may contribute to remedying the AEC by:*
>
> *(a) increasing the transparency of AQR reports, thereby enabling companies and shareholders to assess better the quality of their existing auditor, compared with other options;*
>
> *(b) increasing, in combination with other remedies, a company's bargaining power outside the tender process; and*
>
> *(c) making a company more likely to switch auditors, thereby increasing rivalry.*

We comment as follows:

1. We have no objection in principle to the FRC being given a secondary duty to promote competition between audit firms and beyond the current "Big Four";
2. We do not think that it is a sufficient condition on its own to achieve significant change in audit tendering or rotation of audit firms;
3. We would welcome increased transparency of AQR reports, but do not think that this increased disclosure around the AQR reports alone would significantly influence company behaviour in

appointing or reappointing auditors. Moreover, this increased transparency could be achieved more directly through an explicit requirement that they are made available to shareholders (as proposed in our response to the proposed remedies dated 19th March 2013;

4. We do not understand how such a new duty for the FRC would make companies more likely to switch auditors. In its exercise of the new duty, the FRC is more likely to seek to influence auditor behaviour whereas the AECs identified in the Commission's summary of Provisional findings showed clearly that it is the behaviour of companies in reappointing the same firm for long periods that is the behaviour that needs to change.
5. We would, further, like to draw attention to the importance of regulatory independence for effective oversight of competition. The FRC's independence from the auditing profession has been questioned in some quarters for drawing heavily on accounting firms staff (past and present) for professional input. The issue of regulatory capture was raised in the UKCC's original "*Issues Statement*" (Dec 2011), and would need to be dealt with in the event that it was awarded a competition mandate. Of course, it is also a matter of concern under its current mandate.
6. In summary, whilst we are not necessarily opposed to this remedy, it is our view that if the FRC is given the secondary duty to promote competition, this is unlikely to make a material difference in tackling the underlying incentive problem and lack of accountability to the final customer: shareholders. It remains vital that audit firms' tenure at companies is capped, and we would urge the UKCC to consider the additional remedy to limiting non-audit or audit related work undertaken by the auditor to further reduce the underlying source of perverse incentives.

Yours faithfully,

Elizabeth Fernando, Head of Equities

USS Investment Management

Eric Tracey, Partner

Governance for Owners

Frank Curtiss, Head of Corporate Governance

RPMI Railpen

Sacha Sadan, Director of Corporate Governance

Legal & General Investment Management

Mike Taylor, Chief Executive, **London Pensions Fund Authority**

Robert Talbut, Chief Investment Officer

Royal London Asset Management

Mark Fawcett, CIO

National Employment Savings Trust (NEST)

Henry Boucher, Deputy Chief Investment Officer

Sarasin & Partners LLP

RA Collinge, F.C.A., Head of Corporate Governance

UK Shareholders' Association

Alan MacDougall, Managing Director

PIRC Ltd (European Corporate Governance Advisors)