MAZARS

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Dear Sir

Audit Market Investigation - Evidence relating to the selection process: tendering, annual renegotiations and switching

1. Introduction

Mazars, the integrated international audit and advisory organisation with 14,000 professional staff in 69 countries, is pleased to submit its comments on the above working paper.

Our comments focus on your key initial indications as set out in paragraph 2 of the working paper.

2. Winning engagements without professional tenders

You indicate in paragraph 2(a) that 'in the vast majority of cases audit firms gain FTSE350 engagements by participating in competitive tenders'. We are uncertain about this initial indication.

In paragraph 28 PwC indicate that from time to time companies became its client prior to listing on the London Stock Exchange without a tender. In the next paragraph, it is stated that in the period 2006 - 2011 Deloitte and KPMG became the auditor of eight and nine companies respectively without a formal tender, in Deloitte's case it is indicated that they were already auditor before the companies concerned were listed. Given that each year only roughly nine companies change auditor in the FTSE350 (see paragraph 182) the number winning engagements without a tender may not be that insignificant a proportion of the total. Those awarded without a tender would be particularly worthy of attention if, as seems to be the case, some were appointed just before listing as there is significant concern that investment banks sponsoring IPOs, brokers and other advisers push companies towards the Big 4 as part of the listing process where they are not already using one of them as their auditor.

3. Tenders are very infrequent- on average less than four times a century in a FTSE100 company

We strongly endorse your initial indication that tenders are infrequent in the FTSE350, with paragraph 93 indicating that each year only 3.6% of FTSE100 companies and 4.2% of their FTSE250 counterparts held a tender process with regards to their audit during the period from 2007 to 2011.

If the above rates are constant over time, a FTSE100 company will have a tender approximately once every 28 years, less than four times a century, and a FTSE 250 company once every 24 years, hardly a sign of a vigorous competitive market.

With regards to paragraph 120 of the working paper, Table 7 shows that GT won one FTSE100 tender in the period 2007 to 2011.Unless there was a timing issue with a company dropping out of the FTSE100 post tender but prior to audit, we were not aware of GT being the auditor of a FTSE100 company in the period though conversely we understood BDO undertook one FTSE100 audit and they are showing as not having won any FTSE100 tenders in the period, which may, of course, be the case if they were already the auditors..

4. Threats to tender leading to fee reductions- a further sign of a less than active competitive market

A number of the Big 4 emphasise that even where there have not been tenders there have been many 'threats' to put the audit out to tender. You observe in paragraph 2(e) that where companies have adopted such strategies this has led to a reduction in the proposed audit fee. This does not seem to be the sign, at least *prima facie*, of a market in which the fee is set on an ongoing basis at a level that you would expect if it were actively competitive especially as you also report in paragraph 70 that 'incumbent auditors that participate in tenders usually offered a significant reduction in the fee'.

5. Caution needed with regard to tender costs to firm

We are surprised at the comment that tender preparation costs to the firm represent 'on average roughly 20% to 60% of the first year's audit fees'. We firstly note that these costs generally seem to be based on applying normal charge-out rates which involves an element of double counting as the charge-out rates take account of the fact that not all hours are chargeable. We also note that the methods of determination of the estimates do not appear very precise, sometimes involving recollection of hours spent a substantial time after the event. The upper end of this very broad range, namely 60% of the first year's audit fee, would appear hard to justify in other than very exceptional circumstances.

6. Hard to understand mean length of tenure when compared with switching rates

You report in paragraph 2(f) that on average 3.3% of FTSE350 companies switch auditors each year which you rightly describe as 'a small minority'. Among FTSE100 companies the switching rate is even lower at 2.4% over the period 2000-2011 and the earlier Oxera research found that it was similarly low dating back to the 1990s. A constant rate of switching of 2.4% per annum would suggest that a company would on average retain its auditor for 41.6 years, which broadly accords with similar calculations made for the FTSE100 by others.

We do not believe your figures in paragraph 2(f) suggesting that the average tenure for FTSE100 auditors is just 13 years and for FTSE350 companies even less at roughly 11 years are reliable when the previous paragraph suggests that for FTSE100 companies it should be of the order of three times as long.

We would make two points. Firstly, the meaningful figure to calculate is the mean of the length of tenure of the auditor at each FTSE100 company rather than the mean tenure for the FTSE100 index as a whole at a particular point. Auditors are appointed to companies on an individual basis and thus the relevant mean is the aggregate of the total tenures divided by the number of companies rather than slicing the index at any one date.

To illustrate the difference, if auditors on average were in office for 50 years and there was a constant annual switching rate of 2% the mean tenure for the index at any one point would be 25 years as some would have just started their 50 year period and others would be close to the end of theirs.

The second vital point is that as discussed in our response to the working paper on Descriptive statistics is that we believe there is a serious flaw in the methodology you have adopted for estimating the tenure where relevant data is missing.

In view of the importance of understanding the length of audit tenure at each company, in the FTSE100, we would suggest you write to each company and ask them to formally advise you of when their current auditors were first appointed and to provide supporting evidence by including a copy of the relevant financial statements or record of the relevant AGM. This will provide you with reliable information on the number which have had a very long tenure and the length of that tenure- at the moment there are oft quoted references to one or two companies which have had their auditors for over a hundred years but it would be helpful to get a reliable picture as regards each FTSE100 company.

7. Seemingly different views on the value audit clients attach to non-audit services

In Annex 1 on page 63 you report on the Big 4's views on the value audit clients attach to the supply of non-audit services by the audit firm. They generally seem quite positive about the merits of providing other services and this is borne out by them still representing a significant proportion of the audit fee for FTSE350 companies, albeit less than in earlier years. In seeming contrast, FTS350 companies professed that they did not rate a firm's ability to provide non-audit services very highly in selecting their auditors. It may be worthwhile exploring this issue in a little more depth.

8. Further discussion

If you would like to discuss further any of the issues covered in this paper, please do not hesitate to contact David Herbinet, Global Head of PIE Audits, on 0207 063 4419 or Anthony Carey on 0207 063 4411.

Yours faithfully

Mazars LLP

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