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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 comments on the Competition Commission's (CC) provisional decision on the remedies which it intends to introduce to deal with the adverse effects on competition (AEC) which it has identified in its provisional findings into the market for the supply of statutory audit services to large companies in the UK.

The principles and potential remedies which are under consideration by the CC reflect concerns raised by many stakeholders about the structure of the UK large company audit market. We believe that the introduction of a reasonable and proportionate package of remedies will bring about enhanced competition leading to better outcomes for customers, particularly for investors, and would facilitate an increase over time in the number of audit firms with a meaningful share in the market for large listed company audits.

Provisional decision on remedies
In our view the CC has presented compelling evidence of the need for intervention in this market. Subject to the detailed comments set out in the Appendix to this letter, we believe that the package of remedies provisionally decided by the CC is a reasonable step in the right direction and has a realistic prospect of addressing the concerns which the CC has identified, as long as it is introduced as a package in totality.

However in our view the package would be even more effective if additional provisions were included. We believe that the package of remedies which is being provisionally recommended for implementation by the CC is less effective as a result of the omission of three measures: namely (i) mandatory audit firm rotation (MFR), (ii) further constraints on the supply of non-audit services by the incumbent auditor, and (iii) the introduction of either mandatory or incentivised consortia audits. Absent the introduction of some or all of these measures, we are concerned that the package is too reliant on voluntary changes in the buying habits and behaviours of customers, and therefore risks not being fully effective in addressing the concerns stated by investors and identified by the CC.

We have set out in the appendix the detailed reasons why we think these additional measures would further benefit customers. In particular, we are unconvinced that mandatory tendering without the inclusion of a back-stop period by which companies must switch auditor will have the desired effect of leading to many more auditor switches in the market and therefore addressing investor concerns over the current length of audit tenures in the FTSE 350. The evidence presented by the CC in the Provisional Findings report shows that it is the actual process of switching which gives rise to benefits to customers (e.g. in terms of lower prices), and not the tendering process *per se*. Whilst more tendering is to be welcomed, we believe MFR would have provided the added insurance necessary to ensure that the benefits of switching materialise in practice. We are also cognisant that the introduction of MFR, as proposed by the European Commission, has attracted significant support from stakeholders, including investors.

We believe that the proposed interventions (including the additional remedies we believe are necessary to ensure the package is fully effective) need to be taken together and considered in aggregate. The proposed remedies are not mutually exclusive and no one remedy will bring about sufficient change in the market alone. In our view it is therefore essential that a balanced package of remedies is introduced, which together will bring about positive change for customers. We therefore strongly support the CC's proposal for a range of remedies, and would urge the CC to reconsider the additional remedies which we believe are necessary to address the identified AEC and introduce effective competition into the large company audit market.

Further, we believe that for many of the proposed remedies their effectiveness (singly and taken together) will be significantly impacted by the precise way in which they are implemented. In our view, getting this detail right is critical. We set out in the appendix to this letter our views in this regard.

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 – Grant Thornton views on the CC's provisional decision on individual remedies

Remedy options that the CC is proposing to take forward

1. ***Mandatory tendering***

1.1 As set out in our response to the CC's remedies notice, Grant Thornton supports the adoption of measures to prevent complacency by audit firms in a market where audit tenures are excessively long and which will bring about improvements in innovation, quality and price through increased competition.

1.2 We also agree with the concern expressed in the CC's provisional findings that, in the absence of a more regular and formal process for assessing the quality, price and innovation of alternative providers of statutory audit, companies have limited visibility of the capabilities of those firms with which they have no existing audit relationship[1].

1.3 The introduction of mandatory tendering will help to remedy this concern. In particular, mandatory tendering ought to help to create an environment in which audit committees (ACs) plan ahead for a tender process which they know will be coming, and therefore are incentivised to get to know other firms in advance. More companies should therefore understand the qualities and capabilities of a wider range of firms, and in turn have more meaningful bargaining power in the auditor appointment process. Mandatory tendering also takes away the "whether to tender" decision from management and so better aligns auditor incentives with those of shareholders, as opposed to management. A regular tender process also provides a forum for a substantive review of how the audit is conducted and provides increased assurance to shareholders that the auditor selection process is robust, even in a situation when the incumbent audit firm is retained as auditor. An increase in tendering therefore plays a part in improving the input of ACs (and Audit Committee Chairs (ACCs)) in the tender process and in enabling the audit product to meet better the requirements of shareholders and investors.

1.4 We concur with the CC's opinion that an almost inevitable outcome of more frequent tendering is that the unit costs of tendering will fall as companies and audit firms become more familiar with efficient and effective tendering processes. For example, in a market with, say, 35 – 70 tender events a year audit firms would be forced to focus their tender efforts solely on audit quality and not the other matters

[1] See Grant Thornton response to the CC's Issues Statement.

that often go into the tender effort at present. The competitive process of more regular tendering is also likely to lead to lower audit fees[2].

1.5 However, on its own, mandatory tendering (as part of the package provisionally proposed by the CC) risks being less than fully effective in addressing the adverse effects on competition identified by the CC, as it relies on voluntary changes in the buying habits and behaviours of customers to change the structure of the market – buying habits which to date have resulted in the market which we see today. Grant Thornton therefore advocates that mandatory tendering is accompanied by other measures for it to be fully effective and ensure that the benefits of switching materialise in practice. There is a range of additional measures which would help materially in addressing the risks to audit quality from long audit tenure, and assist in breaking down barriers to entry for audit firms outside of the four largest providers. These options are discussed in more detail in later sections of our response:

a) Mandatory switching (see section 8);
b) Restricting the provision of non-audit services by the auditor of large companies (see section 9);
c) Requiring or adequately incentivising consortia audit (see section 10).

1.6 We support the CC's intention to impose increased tendering in the form of a compulsory order. Whilst we are cognisant of the need to take note of the views of stakeholders, especially shareholders, about whether there is a role for a continuing comply or explain framework (as adopted by the FRC), we agree that a mandatory framework is likely to bring about a greater and more immediate change in the market dynamics. We also support the CC's inclusion of a possible two year extension to the normal mandatory tendering period, which companies can utilise in certain exceptional circumstances (e.g. where a company is facing a financial or reputational crisis, has just acquired a major new business, a major merger or disposal, or where the ACC or CFO/FD has just left the company). The extension will afford companies some practical flexibility to move the tender event if it arises at a time which is unsuitable and could be disruptive to the company.

1.7 It may be useful for the FRC, in updating the UK Corporate Governance Code, to stipulate examples of the kinds of events which they would consider to be "exceptional", and equally examples of events which would typically not be considered to be exceptional. Whilst it will not be possible for such a list to be exhaustive, we consider that it may provide helpful guidance for companies. In situations where companies appear to repeatedly delay tenders, the FRC (or another monitoring body) may want to seek confirmation on the exceptional circumstances that have taken place.

1.8 Regarding mandatory tendering periods, Grant Thornton supported in our response to the CC's remedies notice, along with many investors and stakeholders, a logical approach of audit partner rotation at 5 years (in line with existing requirements for UK listed companies which have little opposition) and mandatory tendering at a maximum of 10 years (being two partner terms and consistent with the FRC requirement in the UK Corporate Governance Code which is well supported).

[2] See CC evidence on the impact of switching on fees.

1.9 We note that the CC have preferred a period of 5 years for the following reasons: "…[the] FRC's judgement [was] that five years was the appropriate interval for rotation of an Audit Engagement Partner (AEP) to ensure their scepticism and independence and see no grounds to alter it. We are persuaded of the benefits of aligning tender periods with AEP rotation, as this would limit the incumbent's advantage deriving from an in-post AEP to lead their bid team"…."In addition, and in line with the FRC's judgement that five years is the appropriate period for the safeguarding of auditor scepticism, we consider that a period of five years would best ensure the sustained alignment of auditor incentives with shareholder (rather than management) demand. We do not, however, consider from a competition analysis perspective that an intra-firm partner rotation adequately secures this position. While partner rotation plays a legitimate role in ensuring that individual audit partners are objective and independent, it does not disturb the economic incentives of the audit firm and it is those firm-level incentives that our analysis is primarily concerned with."

1.10 However, we are not convinced that tendering at intervals as frequent as every 5 years will lead to significantly more auditor changes in the FTSE 350 market than mandatory tendering every 10 years, without the inclusion of mandatory firm rotation at an appropriate back-stop as a means to change the incentives of the buyers of audit services. In our view, increasing the frequency of tendering from 10 years to 5 years is not an appropriate substitute for mandating that companies switch their auditor at some point in time, and will be less effective in achieving the desired outcome (see section 8 for more detail).

1.11 Grant Thornton concurs with a view expressed by many stakeholders that tendering at 5 years may be too frequent, causing unnecessary disruption to the audit market and also restricting the time for the benefits of an auditor's accumulated knowledge to be built up during the firm's tenure, before the perception of objectivity concerns arise. We consider that AEP rotation after 5 years is an important safeguard against independence concerns at the personal level and mitigates the need to consider changing the audit firm at that point. Mandatory tendering every 10 years would limit the incumbent's advantage deriving from an in-post AEP to lead their bid team.

1.12 Perversely, it is likely that more auditor switching would take place under a framework of mandatory tendering every 7 or 10 years than would be the case with a shorter period such as 5 years. This is because many companies and investors have expressed reservations about the cost (and need) for companies to consider changing auditor at 5 years, and so their appetite for change is likely to be lower than it would be at a longer interval. Conversely, the FRC's introduction of 10 year tendering was concluded following consultation with, and wide acceptance by, investors, ACCs, FDs/CFOs, who will therefore have an appetite to undertake a thorough review and to seriously consider changing auditor at this interval. A 7 or 10 year **maximum** period will still allow companies to put the audit contract out to tender earlier if it was considered appropriate to do so.

1.13 A further point to note is that the AEP rotation period of 5 years for listed companies in the UK is not a universal standard, with many countries around the world adopting a period of 7 years (as with current European law and the

international code of ethics for accountants). The point being that the appropriate rotation period for AEPs is not an exact science, with the point at which auditor scepticism needs safeguarding being a subject of much debate.

1.14 Further to the above, we are concerned that if companies and shareholders are not convinced of the merits of switching auditor after a 5 year period, there is a risk that mandating tenders at this frequency will result in companies running a tender process which is not fully embraced (i.e. the tender becomes nothing more than a 'box ticking' exercise to show that the remedy has been complied with). Audit firms may also be dissuaded from entering a tender where they believe that a company has little or no intention of switching auditor but are running a tender in order to comply with the remedy.

1.15 We note the CC's view in paragraph 3.132 that companies have little incentive to run a "sham" tender process because "ACs are now required under the UK Corporate Governance Code to report to shareholders on the approach taken to the appointment and reappointment of the external auditor. The process put in place by the company would need to be sufficiently robust for these purposes" and "as tendering becomes more frequent we expect best practice to become established, so that it will become obvious if any given company departs from expected norms". However these reasons are likely to provide insufficient incentives for a company to undertake a full and open tender process after 5 years if the company has no real appetite for changing auditor at a time when it and shareholders have no concerns over the auditor's independence or objectivity.

1.16 If the CC concludes that 5 year mandatory tendering should be introduced, we advocate that the CC stipulates certain minimum tendering requirements, to encourage a meaningful tender process and to avoid the situation that a tender process is run simply as a formality. The CC makes key points in this regard at paragraph 3.70 (that companies give sufficient attention at the start to the design of the process and that access to senior management is specified and controlled).

1.17 To enable an effective tendering process, and to allow shareholders to provide input to the process should they wish, a company should also be required to announce its intention to tender well in advance of the commencement of the tendering process. Transparency about upcoming tenders will be important also to allow audit firms to prepare and plan well in advance of the tender actually taking place. This is particularly important where a company expects to take advantage of the two year period of flexibility in exceptional circumstances, and during the transitional period when tender events will be linked to the next rotation of an AEP. In the absence of publication, this information is unlikely to be readily available to firms other than the incumbent.

1.18 Grant Thornton is of the opinion that equal access to appropriate information should be available to all firms involved in the tender process in order that the process is conducted in an open and transparent manner. Such information should be sufficient to provide a tendering firm with information to allow their tender and, in particular, fee quote to be as accurate as possible, including the provision of equal access to management. Such a process might include a requirement for a tendering company to send information to those audit firms that it wishes to provide a tender,

including: details of the group structure, reporting requirements, systems, processes and controls, finance team details, Board structure, reporting responsibilities etc.

1.19 With regard to transitional provisions, we support the CC's proposal to link the introduction of the new requirements to the rotation of the AEP, whilst mandating that those companies whose auditor has remained in post the longest, without challenge through a formal tender process, should be the first that are required to put their audit to public tender. The objective should be to have a constant stream of tenders over time, and thereby avoid a flood of tendering in one period and a drought in the next. Linkage to AEP rotation should help to ensure that there is not a significant bunching of new tenders coming to market, but the CC may wish to look at this point in more detail to ensure that the data envisaged in paragraph 3.173 are accurate.

2. *Audit quality review*

2.1 Grant Thornton supports the suggested improvements to Audit Quality Review Team (AQRT) reviews, in terms of the degree to which they allow more effective, and transparent, comparison between different audit firms. If achieved, we agree that this would reduce barriers to switching by improving objective benchmarks of the performance of different audit firms, and thereby assist, over time, in facilitating switching on an informed basis.

2.2 We noted in our response to the CC's remedies notice that more frequent AQRT inspections "across the board" are not necessarily needed in order to achieve this objective. We believe what is important is that the information in AQRT reports that is provided in public reports, and privately to companies, is relevant for informing auditor selection decisions.

2.3 However, we are not opposed to the CC's proposal to ensure that every audit engagement in the FTSE 350 is reviewed on average every five years, with each individual audit engagement in the FTSE 350 reviewed at least every seven years. This increase in frequency of reviews/reports will provide companies with a more frequent company-specific review of the quality of their audit and will also benefit companies and shareholders by providing more information regarding the performance of all firms in the market. The timing of audit review should not be set without regard to the period for mandatory tendering/rotation—for example, it would be unhelpful to conduct an audit review two months into the engagement of a new audit firm following a tender or rotation.

2.4 We support the CC's proposal to recommend that the FRC increase the regularity of AQRT reviews, and reports, on audit firms which are not amongst the four largest firms, such as Grant Thornton, so that those reviews are undertaken at a comparable frequency to those of the four largest firms. The regularity of reviews and the substantive work involved in inspecting audit files of companies of similar or equal size and complexity needs to be consistent as, in the absence of this consistency, the visibility of quality of different firms, for shareholders and companies, is blurred.

2.5 The FRC may need to adopt a framework or guidelines on criteria to consider when assessing the comparability of different companies by reference to their size and complexity, so that companies and shareholders are provided with an appropriate comparable assessment of the quality of the work of different firms – we consider that a split of FTSE 100, FTSE 250 and others may be sufficiently detailed in this regard.

2.6 We would welcome clarification by the CC that the FRC should issue reports on each of the major firms in the same way, to avoid the perception that the largest four firms are different from the others. At present, the reports of the largest four firms are released at the same time under the guise of "Big-4" reports, whilst the other firms are published separately. Our preference would be the issuance of reports on all firms at the same time to remove this implied "grouping".

2.7 Finally, regarding the content of AQRT inspection reports, we support efforts to ensure that AQRT reports refer specifically, where possible, to the output that investors are concerned about, including a review of the ethical practices which the audit firm undertook prior to providing any non-audit services to companies that they audit, and the level of challenge and scepticism which is demonstrated on material accounting issues. We have commented further on this area, under sections 6 and 7 respectively, regarding the public reporting of AQRT reviews by the AC and the ways in which the FRC might amend the AQRT inspection framework and nature of their reviews to meet a secondary duty to promote competition. In particular we comment on the need for there to be sufficient guidance and information on AQRT reports to ensure that review ratings/grades are properly understood and set in context in public reporting.

3. *Auditor clauses in loan agreements*

3.1 Grant Thornton strongly supports the CC's proposal to prohibit contractual clauses placing restrictions on the firms of auditors that may be appointed, which are anti-competitive because they unfairly restrict a company's choice of audit firm. These restrictions exist in many agreements and present unjustified reputational barriers and restrictions on the choice of auditor which are demonstrably not related to capability or quality of the audit firms involved [by reference to inspection reports issued by regulators].

3.2 This remedy forms part of the minimum requirements for the creation of a level playing field for all market participants and would ensure that the auditor selection decision is free from bias and properly informed with regard to audit quality and audit firm capabilities. The prohibition of such clauses will also remove the direct constraint on the ability of companies to appoint an auditor outside of the largest four firms and, over time, will materially assist in reducing the reputational barriers facing auditors outside the largest four firms.

3.3 We welcome the CC's intention to extend the prohibition to "loan agreements which restrict or have the effect of restricting a company's choice of auditor to certain categories or lists of statutory auditors". This will have the effect of prohibiting not just those agreements which specifically refer to the largest four audit firms, but also those that have a similar affect (e.g. a reference to a "reputable

audit/auditor" which is sometimes understood by companies to mean one of the largest four audit firms). Further we welcome the inclusion of the words "or have the effect of restricting…" which, importantly, will mean that the prohibition will cover all such arrangements which seek to influence a company's choice of auditor. One example we have seen is different lending terms, including interest rates, for different auditors.

3.4 The CC's intention to implement the remedy in the form of an Order is appropriate and correct as it is unlikely that non-binding guidance or recommendations would be sufficient to bring the use of such clauses to an end.

3.5 These restrictions also exist, equally importantly, in unwritten form and in agreements outside of the various types of loan documentation referred to by the CC (for example in transaction related contracts such as for the performance of restructuring or due diligence assignments). Grant Thornton has provided evidence of the types of documentation in which we have identified such restrictions in our response to the working paper entitled "Restrictions on entry or expansion". The above practice is also evident with companies aspiring to be public interest entities, where auditors outside of the largest four can be excluded from acting. Grant Thornton therefore recommends that the CC extends its prohibition to all forms of third party anti-competitive restrictions on who a company may appoint as auditor, unless those restrictions can be objectively justified.

3.6 In any case, we recommend that the requirement for companies to monitor and certify compliance with the Order in their Annual Report should be supplemented by further disclosure, also in the Annual Report, of **any** restrictions imposed on the company by third parties regarding the company's choice of auditor, be those restrictions in loan agreements (as defined by the CC) or in any other formal or informal arrangement (this disclosure would go further than the current FRC "Guidance on Audit Committees" which indicates that ACs should disclose any contractual obligations that acted to restrict the ACs choice of auditor). This additional disclosure would send a strong signal to the market that such arrangements (in any form) are unjustifiable reputational barriers and restrictions, and will help to eliminate the risk that those who support such restrictions find new ways to implement them outside of those loan arrangements which are encompassed by the CC's proposed order. It would also allow excluded firms to take informal action, for example engaging with the restricting entity.

4. *Enhanced shareholder engagement*

4.1 Grant Thornton supports changes which will enable greater engagement between companies and shareholders. For this reason we support the CC's intention to introduce, via a recommendation to the FRC, a requirement for companies with a premium listing to "engage with shareholders through seeking shareholder views on audit issues and stating how any shareholder concerns identified as a result may have been addressed; and introduce an advisory vote for shareholders on the sufficiency of disclosure in the Audit Committee Report" and to "update the Stewardship Code to encourage institutional investors to engage with investee companies on audit issues".

4.2 These requirements will reaffirm the need for companies and shareholders to engage on issues relevant to the audit and introduce a requirement for AC's to appropriately react to shareholder concerns or face the prospect of an (advisory) rejection of the sufficiency of disclosures made. However, whilst the CC's proposal is a step in the right direction, there is a risk that the envisaged AC reporting will become "boilerplate" in the situation of shareholder apathy and low attendance at AGMs.

4.3 A further substantive remedy, which would be effective in addressing the issue which the CC has identified, is a requirement for the AC to propose two audit firms to shareholders, following a tendering event, upon which an auditor appointment decision could be made. The AC would be required to provide shareholders with a duly justified preference for one of the audit firms, alongside sufficient information to enable shareholders to make an informed decision. We note that the CC is not inclined to introduce such a remedy due to the difficulties which it envisages that a AC would experience in providing sufficient information to shareholders on which to make an informed decision, and because one firm would need to be on "standby" until after the AGM. In our view these concerns are overstated and could be overcome by clear AC reporting. This remedy would provide a powerful rebuttal of the "IBM factor" which currently exists in auditor appointment decisions, and provide shareholders with an ability to act to change the incumbent auditor where they had unaddressed concerns.

4.4 The CC has provisionally also rejected a requirement for an AGM agenda item for a Q&A dialogue with the AEP and the ACC due to low levels of investor attendance at AGM's. This low level of investor attendance arises, we understand, because many investors consider that there are little, if any, means by which they can engage directly in assessing the audit process. Providing such a forum, accompanied by disclosure by the AC of areas which are a known cause of investor concern, would create a "hook" which investors could use to engage more fully. We continue therefore to support such a Q&A with the audit partner and the ACC to provide a forum for shareholders to engage directly in assessing the audit process and understanding the key areas of focus during the audit. Questions could be sought in advance as a measure to control the process. In much the same way as the company arranges conference calls and internet forums for results announcements, the company could arrange an internet forum between the shareholder group, ACC and the AEP.

5. ***Strengthening the accountability of the External Auditor***

5.1 Grant Thornton concurred with the CC's provisional finding that the incentives of audit firms are often not aligned with those of shareholders. This has occurred over time as the audit model has evolved to the current situation where auditors spend most of their time communicating with FDs/CFOs, some time with ACCs and no time with shareholders, the ultimate customer. However this is not in our view a criticism of auditors or an understatement of a strong corporate governance regime in the UK, but it is more an observation on how the audit role has evolved and the difficulties shareholders have in understanding how the auditor and AC have been discharging their responsibilities to them.

5.2 We supported the CC's proposal to change the relationship of the auditor with company management and with ACs, aiming to increase the independence of the audit firm from management. However in our response to the CC's remedies notice we expressed concerns that the remedy under consideration required further consideration given the inevitability that the relationship between the audit firm and management will be difficult to change given the interaction which inevitably is required during the audit process.

5.3 Grant Thornton proposed that the AC should be given responsibility for a number of areas, including when to tender and rotate (within the constraints imposed by mandatory tendering and/or rotation), the tender process including which firms should be invited, auditor appointment and remuneration and liaison with shareholders on audit aspects, including auditor selection. We welcome the CC's intention to introduce these requirements via an Order, along with a requirement that only the AC/ACC can agree the scope of the audit work and authorise the external audit firm to carry out non-audit services (NAS).

5.4 Further, we support the CC's amendment to the possible remedy set out in its notice of remedies to make it more practicable by setting a requirement for the AEP to report, as soon as is practicable, any audit issue that is considered to be material "having established the facts of the issue with finance or other relevant company staff". This amended proposal is a positive development which will give the AC timely oversight of key audit issues and decisions whilst acknowledging that company finance staff, including the FD/CFO, are necessarily involved in the "day-to-day" practicalities of the audit. Clearly, the issue of materiality of the issues that should to be reported to ACs will be relevant to the effective implementation of this remedy.

5.5 We consider that these changes can be achieved by building on the current guidance on the role of the AC and without materially changing the legal duties of the Directors and the Board of the Company, by giving the AC these responsibilities, and specifying that the AC is acting on behalf of the Board.

5.6 The most significant cost of implementation of this remedy will be any additional resource or procurement assistance which would be required for AC's, although we doubt that this resource requirement would be significant given the fact that many ACCs are former auditors/accountants themselves who have sufficient familiarity with the processes they would be undertaking and that the occurrence of tendering and rotation requirements is unlikely to be frequent enough to require a significant uplift in ACC resource.

6. *Extended reporting requirements – in both the AC's and auditor's report*

6.1 Grant Thornton supports efforts to improve reporting in the AC or Auditor report to meet the demands of investors. The quality of reporting by companies, and audit reporting thereon, can be a direct signal of quality to shareholders.

6.2 We concur with the CC's intention to recommend certain requirements to the FRC, which is best placed to address this issue with UK companies and shareholders, and

who we would like to acknowledge have already introduced a number of areas of enhanced reporting in recent years, both by ACs and auditors.

6.3 The CC recommends reporting on three key points, by the AC – "the AC should report on (i) whether the AQRT has concluded a review on the audit of the company's financial statements in the reporting period, (ii) what the principal findings were, including grade, and (iii) how both the AC and auditor are responding to these findings. The CC considers that "there are merits in allowing the AC an opportunity to explain to shareholders what steps it has taken to respond to a poor AQRT grade to ensure the effectiveness of external audit".

6.4 We concur with the above proposal which should provide greater visibility for shareholders of audit quality, as determined by the AQRT. However, as set out further in section 7, we consider that the FRC will need to adapt the framework and nature of their reviews in order to allow greater comparability between audit firms and so that AQRT reports refer specifically, where possible, to the output that investors are concerned about, including a review of the ethical practices which the audit firm undertook prior to providing any non-audit services and the level of challenge and scepticism which is demonstrated over material accounting issues.

6.5 Absent these changes, we are concerned that the work performed by the AQRT, and the grading process for AQRT reports, will continue to be insufficiently understood, with significant scope for misinterpretation of a grade or rating, particularly by those less familiar with the process. AC's and shareholders will therefore need sufficient guidance and information to ensure that grades are appropriately understood and reflected in context in public reporting, to avoid auditor appointment decisions being made on the basis of incorrect assumptions.

6.6 Whilst Grant Thornton is supportive of the CC's recommendation, we believe that reporting by the AC should go further, so that ACs are explicitly required to give due consideration to, and provide disclosure of, their policy for using firms other than the incumbent auditor for non-audit work, and for using more than one audit firm in the group audit. Disclosures in these areas would break down barriers that currently exist for audit firms in the market, and provide shareholders with more transparent information about the audit firm's engagement with the company, and the company's actions to ensure that the audit firm is independent.

6.7 In this regard, we recommend that the CC provides a further recommendation for the FRC to introduce explicit reporting requirements for companies with a premium listing to state in the annual report, the following information where relevant:

- the company's approach to the audit tender and audit firm selection decision, including its approach to re-tendering (and likely timing of future tenders due to the mandatory tendering proposals);
- the company's policy on maximum auditor tenure, and the period until mandatory audit partner rotation (and tendering based on current CC position);
- any restrictions imposed on the company by third parties regarding the company's choice of auditor;

- the company's policy for using a range of accounting firms, and details of how they get to know and use accounting firms which are not among the dominant firms;
- the company's policy for using its auditor to undertake non-audit services, including any limits imposed on the volume of non-audit services provided by the auditor, services which may be provided by the auditor but only with prior approval of the audit committee, and use of firms other than the auditor; and
- the company's approach and policy for ensuring that sufficient engagement/dialogue is had with the company's shareholders in the above areas.

6.8 These disclosures should be the responsibility of the AC. The principal benefit of these additional disclosures would be to improve the transparency for shareholders of how the company engages with the auditor and ensures that the audit firm is independent of management. This would help to break down the misalignment of incentives which the CC has noted is currently in place.

7. ***Competition objective for the FRC***

7.1 We support the CC's intention to implement this remedy, as set out in our detailed comments in our response to the CC's notice of a further possible remedy[3]. We see the additional secondary duty of the FRC to promote competition as being consistent with good regulatory practice and in line with developments in other areas of regulation, and in particular with other professional services regulation. These duties reflect a recognition that, where the regulator has a requirement to promote competition, this can be expected to have a positive impact on the delivery of services to users. A competition objective would also give the FRC a firmer base on which to take appropriate action to address the 'muted forces' of competition that have provisionally been found to exist, as noted by the CC. As the FRC has already expressed concern about how it would fulfil the competition duty,[4] we trust that the CC will have dialogue with the FRC as to how to put in place the appropriate resources and framework to fulfil this duty.

7.2 The CC suggest that the FRC might use the secondary duty to promote competition by, for example, "modifying the scope of AQR investigations and reports to make them focus on a wider range of FTSE 350 companies and statutory auditors"... and…"an alternative approach [to AQR reporting] might be to inspect the audits of a wider range of FTSE 350 companies—i.e. a selection not limited to those judged to be the most complex and risky, but including inspections of companies which may be considered typical of the FTSE 250 rather than the FTSE 100. Such an approach would still focus on the quality and innovative aspects of the audits, but may enable the FRC to make such reports capable of being used by companies and ACCs to make some comparisons between rival audit firms."

[3] http://www.competition-commission.org.uk/assets/competitioncommission/docs/2011/statutory-audit-services/130628_notice_of_possible_remedy_grant_thornton_response.pdf
[4] http://www.competition-commission.org.uk/assets/competitioncommission/docs/2011/statutory-audit-services/130628_notice_of_possible_remedy_frc_response.pdf

7.3 This suggestion is consistent with our previous submissions, where we have expressed support for the introduction of improved AQRT reports, in terms of the degree to which they allow more effective and transparent comparison between different audit firms. Increasing the comparability of different audit firms operating in the FTSE 350 would reduce barriers for companies to switch by providing them with relevant information to assess alternative suppliers. This would be particularly pertinent for shareholders who currently have very limited ability to compare alternative audit firms. It may be appropriate for the FRC to take this opportunity to consult with ACs and shareholders on the range, type and format of the information required so that the information reported is of maximum benefit to ACs and shareholders in making an informed decision in relation to the merits of the different auditing firms.

7.4 The FRC currently conducts both "thematic reviews" and "firm reviews"; the latter focusing on specific company audits, whereas the former deals with key audit issues, germane to a number of audits conducted by all firms (e.g. ethics, group audits, letter box companies etc.). The FRC's primary focus on "firm reviews" could present issues when reporting findings for smaller audit firms who have fewer clients within the AQRT remit, as it will become increasingly obvious which companies' audits have been reviewed at those smaller audit firms. Further, under the current AQRT review regime, those companies with a smaller audit firm are likely to be selected for AQRT review more regularly than if they were being audited by a larger audit firm (we note the CC's intention to recommend that all companies are reviewed at least once every 7 years in the future).

7.5 Accordingly, we would recommend that the FRC's primary review approach is a "thematic" one, focusing on the same audit "theme(s)" (rather than audit client) across all 9 major firms, to provide comparability without revealing the identities of the reviewed audit clients. However, as noted at section 6.3, we support the CC's intention for, at the specific company level, the AC (as opposed to the AQRT) to report on the findings of AQRT reviews and ratings. There may also be other ways in which the FRC can achieve greater comparability between reports on audit firms and we would be happy to contribute further to any discussions in this regard.

7.6 We also considered some further practical steps that the FRC might take were the remedy to be implemented. One suggestion was to increase the regularity of AQRT reviews on audit firms which are not amongst the four largest firms, such as Grant Thornton, so that those reviews are undertaken on a comparable frequency to those of the four largest firms, where companies of a comparable size and complexity are being audited. We note that this suggestion has been taken forward and is being recommended by the CC at remedy 2.

Remedy options that the CC are not minded to pursue

8. ***Mandatory switching***

8.1 The evidence presented by the CC in the Provisional Findings report clearly shows that it is the actual process of switching which gives rise to benefits to customers (e.g. in terms of lower prices), and not the process of tendering *per se*. In this regard, the CC has found that:

(a) "switching auditor is typically associated with a fee reduction" [Paragraph 1.35 of Provisional Decision on Remedies];

(b) "the results indicated that audit fees generally decreased in real terms the year after a switch" [Paragraph 7.39 of the Provisional Findings report];

(c) audit fees per hour decrease following a change in auditor [Paragraphs 91 to 96 and Figure 17 of Provisional Findings report, Appendix 5]; and

(d) the CC's survey showed that of those FTSE 350 companies that had switched in the last five years, 52% noted that switching auditor resulted in a lower fees, and 48% noted increased quality, with 20% reporting both reduced fees and improved quality [Provisional Findings report, Appendix 3, paragraph 67].

8.2 However, despite the CC presenting compelling evidence in relation to the benefits of switching (as distinct from the tendering process), the CC has decided not to pursue MFR. As noted in section 1, we do not believe that mandatory tendering, of itself, will be fully effective in changing the buying decisions of companies. This relies on a "leap-of-faith" that more frequent tendering will result in behavioural changes which in turn will lead to more frequent switching. Grant Thornton supports increased tendering coupled with a back-stop measure of MFR, at a suitable period, to encourage companies to build relationships with new firms, and mandate that a fresh-pair of eyes is required after a certain amount of time. This would also provide the added insurance that the benefits of switching identified by the CC are realised in practice (in the event that mandatory tendering alone does not lead to more switching).

8.3 Implementation of MFR alongside more frequent tendering, which is a position supported by many investors[5], addresses the risks that arise when an audit firm has been in place for too long. While the current requirement for audit engagement partner rotation is an important safeguard for these concerns at the personal level, it is clear that it does not on its own address the perception that a familiarity threat arises between the company and the audit firm.

[5] See an investor letter signed by large institutional investors and investor associations managing assets of > €2trn - http://www.uss.co.uk/Documents/Audit%20-%20Group%20position%20paper%2022%20Feb%202013.pdf

8.4 In terms of a time period for MFR, we support 15 years, which is also widely supported by other investors and stakeholders. Grant Thornton has been engaged in discussions around the world on mandatory firm rotation and has seen 14 or 15 years as a time period which is not considered inappropriate by many who support a fixed rotation period. In the European context, 14 years is two terms of European audit partner rotation limits of 7 years. The CC may consider therefore that 15 years is a more "logical" period for mandatory rotation of audit firms in the UK, being 3 audit partner terms of 5 years.

8.5 We note that MFR appears to be supported by most European legislators and has received wide support by many investors groups, who believe that it will address a significant customer concern about the current length of audit tenures. This is acknowledged by the CC at paragraph 2.24 of the Provisional decision on remedies.

8.6 There are also many examples in the public sector, where the largest entities are at least as large and complex as many FTSE companies and more complex than most, which indicate that frequent switching goes hand in hand with strong audit quality[6]. Our understanding is that increased frequency of audit firm rotation in the public sector has also encouraged value for money and improved audit quality and service for the institutions involved.

8.7 We note that the CC has provisionally decided not to proceed with a MFR remedy for the following reasons:

a) mandatory switching would exclude the incumbent from the competition for the engagement once its term expires and there would be a further loss of efficiency if the incumbent would have been the preferred bidder at that point; and

b) mandatory tendering, combined with the other remedies suggested, is considered to provide a more proportionate and effective package.

We consider each of these arguments in more detail below.

8.8 First, the CC's conclusion that excluding the incumbent from the competition for an engagement could result in a company having insufficient alternatives appears to be informed on the basis that there are only four potential suppliers in the market, which would be reduced to three if the incumbent were unable to compete (and to two if another supplier was conflicted from competing). However, in the case of the vast majority of the FTSE 350 companies, there are already more than four firms who have the capabilities to provide such audit services. The exclusion of the incumbent from bidding for the engagement would simply result in the gap being plugged by other auditing firms, which would be good for competition.

8.9 Further, this reason for not introducing MFR is somewhat counter-intuitive in the sense that it is made on the basis of the characteristics of the existing market structure, which the CC has found to result in an AEC. Rotation should be expected

[6] See the Audit Commission's 2012 Quality Review Programme report at http://archive.audit-commission.gov.uk/auditcommission/SiteCollectionDocuments/AnnualReports/2012/20120621-quality-review-programme.pdf.

over time to result in an increased number of providers of audit services to the large company audit market thereby introducing additional choices and greater competition for FTSE 350 companies.

8.10 We believe that the conclusion that MFR harms competition, by excluding the incumbent, is too simplistic as it ignores the beneficial effect which comes from changing buyer behaviour and habits at intervening tenders (i.e. which includes tenders when the incumbent is not excluded). Since the buyers of audit services (company management) are not the true customers of the audit product (who are the shareholders), it is important that buyer habits favour protecting investors' interests. MFR is a means to influence buyers' behaviour by increasing their appetite to consider alternative audit firms from the incumbent, in the knowledge that ultimately a change would be required at some defined point in the future. In the case of a company that is minded not to change auditor despite the wishes of its shareholders, tenders may currently be conducted in perpetuity if there is no real appetite for change. However, if tendering is introduced alongside a back-stop date when a switch in auditor must be made, companies would be incentivised to build relationships with alternative suppliers and firms would be further incentivised to enhance their capabilities where they believe there is a realistic chance of success.

8.11 However companies, in their responses to the CC, have been critical of the introduction of MFR and have provided a number of reasons why they consider that mandatory switching would be a problem. Paragraph 4.21 of the CC's Provisional decision on remedies notes:

"All the FTSE 350 companies that responded to the Remedies Notice opposed mandatory switching. They said that this would be highly disruptive and could compromise audit quality. Some said that the risks associated with mandatory switching would be likely to outweigh the benefits. The reasons given for these responses included: it would take time for a new auditor team to fully understand the business; a new auditor that was less familiar with the business would be less able to provide a robust challenge to management; the balance between the benefits of continuity and renewed challenge were appropriately met by the requirement for partner switching; 'educating' the new auditor would be a significant burden on management; the options for switching were limited by the impact of other NAS received by the company from other providers; and the switching of auditors would have a knock-on effect of requiring switching of these other services."

8.12 Each of the points made above applies equally to introducing a new auditor following a tender process as they do to a mandatory change in auditor. This suggests to us that mandatory tendering, on its own, will not significantly affect companies' appetite to change auditor, as most companies have expressed an unwillingness to change auditor owing to the cost and the "burden" which management consider it places on the company, and to the loss of accumulated experience which rests with the incumbent auditor. This means that the benefits of switching that have been clearly identified by the CC may not occur in practice if mandatory tendering is implemented without MFR. This also suggests that, contrary to the CC's suggestion, mandatory tendering (combined with the other remedies suggested in the PDR) will not be as effective a package of remedies as one which also includes MFR, which will ensure that switching does actually take place.

Therefore regulatory intervention through the introduction of mandatory switching is needed to create a real change in customer buying habits.

8.13 A further argument in favour of the need for MFR is that the likely result of tendering, on its own, is that the incumbent will always be in an advantageous position, principally through the eyes of a buyer who is concerned at the impact on management time of changing auditor and who perceives that there would be a significant loss of the incumbent's accumulated knowledge and experience if they decided to switch auditor. Therefore excluding the incumbent from a competitive tender at an appropriate point is not an unhealthy scenario because competition is likely to be healthier between two (or more) firms when neither is the favoured incumbent and they can compete on a level playing field on all parameters.

8.14 Paragraph 4.50 states "the costs to FTSE 350 companies of switching auditor were material in the context of the bargaining position of these companies in their annual negotiations with their incumbent auditor". However, it is unlikely that the costs of rotation to companies are significantly different from those of tendering since the most significant costs, those of preparing the tender and familiarising the audit firm with the company to a level which allows an appropriate presentation and tender to be made, are borne during the tender process. Additional costs which would be incurred owing to a rotation requirement would include the opportunity cost of management time spent familiarising the new auditor with the company and its systems and internal control processes. Whilst Grant Thornton is not best placed to provide details of the time involved in this process (which invariably will be different depending on the complexity of the company), it seems very likely that the time spent by companies would be significantly less than that the auditor spends in familiarising themselves with the company (on the basis that the management already understands its business and the audit firm will be the one making the most significant investments in familiarising itself with the company).

8.15 The CC notes at paragraph 4.49 that with the proposed remedies package "we would expect companies to switch auditors more often than has been the case in the past", and at paragraph 4.11 that "mandatory switching might be considered necessary if there was an expectation that mandatory tendering would be ineffective or not fully effective".

8.16 In view of our comments above, and in the situation that the CC concludes that MFR is not necessary at this stage, we consider that the Competition and Markets Authority (CMA) should be required to consider the efficacy of mandatory tendering in achieving its policy objectives in due course. At that stage, if mandatory tendering on its own has not been found to be fully effective, MFR should be reconsidered as an additional measure to address investor concerns. In this regard, we would encourage the FRC to monitor and publish details on the levels of switching amongst the FTSE 350 firms that take place on an on-going basis in order to monitor the effectiveness of the proposed package of remedies. If levels of switching and competition do not materially increase as a result of these proposed measures, we would recommend that the large company audit market is referred back to the CMA, with a possibility of MFR then being introduced.

8.17 Finally, any departure from the status quo will almost certainly attract some form of criticism. The claimed costs of potential changes are often overstated (and benefits understated) in advance of a measure being adopted. However once the change is adopted very often the market comes to accept that the change was beneficial. For example, when the proposal for 5 year audit partner rotation was first mooted, there were concerns about the cost of implementing such a requirement and also over the potential impact on audit quality of overly frequent change. These outcomes did not materialise in practice and there has not been any contention, of which we are aware, that consequently either audit quality has fallen or that costs significantly increased for companies or their shareholders. However, market forces have not led to desired levels of liquidity and instead have caused investors to question the adverse impact on audit quality of long periods of tenure. Changing auditor too frequently may not be optimal, but never, or rarely, changing auditor does not meet investors' demands either. The desired result lies somewhere in between. When market forces do not deliver a desired adverse outcome then regulatory intervention becomes appropriate. Given the opposition expressed by many companies to changing auditor, we believe that audit firm rotation should be required by law.

9. ***Constraints on the provision of Non-Audit Services (NAS)***

9.1 Grant Thornton continues to be of the view that the CC should implement a remedy which places further constraints on the ability of the incumbent auditor to provide NAS to the company. This remedy would be effective, alongside other remedies, in reducing the barriers to switching identified by the CC. Moreover, such a remedy would be straightforward and cheap to implement.

9.2 The UK listed audit market currently follows the Ethical Standards issued by the Auditing Practices Board which build on the IFAC Code of Ethics and which stipulate various requirements regarding the provision of NAS by the auditor. These ethical rules prohibit the provision of certain non-audit services which, if provided by the auditor, are considered to give rise to a threat to independence or objectivity. In addition, they set parameters in relation to the size and type of fees which are able to be charged. In many cases NAS are able to be provided by the auditor if appropriate safeguards are applied and the AC gives approval to the service provision.

9.3 Notwithstanding the above regulations, for many companies the default provider of non-audit services is currently the incumbent auditor. Grant Thornton's research into corporate reporting within the FTSE 350 "The chemistry of governance, A catalyst for change" indicates that on average companies in the FTSE 350 incurred non-audit fees of 68% of their audit fees in the period from May 2011 to April 2012 and, of these, many still paid more to their auditor for NAS than for audit services.

9.4 Whilst the introduction by the CC of a remedy meaning that only the AC shall negotiate audit fees and award NAS contracts to the external audit firm will reaffirm and mandate existing guidelines (and may be expected, given the responsibility of the AC to protect independence and scepticism, to further reduce the levels of NAS purchased from companies' external auditors), it is unlikely to lead to a significant shift in the market given that most large one-off NAS assignments, such as tax consultancy and acquisition due diligence services, will still be able to be awarded to

the incumbent audit firm. The award of such NAS contracts is justified by many companies by the auditor's experience and knowledge of the company and, assuming safeguards are applied, is not in itself a threat to the auditor's independence. However in this environment it is very difficult for firms other than the auditor to build relationships and raise their profile with the company.

9.5 Grant Thornton supports greater restrictions on the provision of certain types of NAS and/or limiting the aggregate level of fees from such services that are able to be provided to FTSE 350 companies by the incumbent audit firm as a means for companies to get to know more firms (via the provision of NAS) and, over time, increase the number of potential providers of audit services that have experience of the company. A restriction on the provision of NAS by the audit firm will also improve the perception of auditor independence, as supported by many investors, and it would positively impact on market liquidity.

9.6 The CC asserts in its reasons for not proceeding with this remedy that "there is a risk that if greater restrictions were placed on NAS provision by the external auditor, other firms would necessarily undertake more NAS and might be disinclined to participate in [audit] tender processes thus reducing the level of competition". We believe that this concern is overstated as the benefit that a firm might derive from a (likely 5 year minimum) audit contract, together with a minimum 5 years of NAS work which the AC is satisfied can be performed by the incumbent auditor, is likely to exceed the fees from potential NAS assignments which may be available during that period to other firms.

9.7 For the reasons set out above, we believe that both prohibitions on certain services (primarily tax consulting, due diligence and business risk services which are typically transactional in nature and constitute a significant proportion of NAS provided by the auditor to the company) and limiting the aggregate level of NAS by reference to the audit fee (for example, 50% of the audit fee, averaged over three years) merit deeper consideration. Grant Thornton considers that this remedy is a low cost measure to changing buying patterns in the market, as the remedy essentially replaces one supplier with another in markets where there are ample suppliers.

9.8 We note that this remedy has also attracted significant support from legislators in Europe, with the European Commission proposing an enhanced list of types of NAS which the auditor would be unable to provide and a cap of 10% of the statutory audit fee on the provision of "allowed" NAS by the auditor. At the time of writing, our understanding is that an enhanced list of NAS by type of service and a cap of 70% of the statutory audit fee (averaged over three years) is also being supported by most Member States in the on-going discussions.

10. *Joint or component audit*

10.1 As set out in our response to the CC's remedies notice, Grant Thornton considers that in order to bring about the desired change in market structure by rectifying the unnecessary market imbalance which is in favour of the largest firms and thereby facilitate a quality audit product to better meet shareholder demand, there should be

an incentive for companies attached to consortia audit arrangements[7] (also referred to as component audit). Incentives for a company to use more than one firm for its group audit arrangements might include an increased MFR period (say 21 years instead of 14 years) or the ability to use the incumbent audit firms for an increased range of NAS.

10.2 This remedy would help to overcome one of the issues identified by the CC, that mid-tier firms face barriers to entry in the market. We believe that, over a period of time, the introduction of consortia audits would facilitate the recognition that a wider range of firms is capable of auditing the largest companies, and thus facilitate the involvement of more audit firms in the audit of large listed groups. This should also reduce the impact of the failure or withdrawal from the audit market of one of the largest auditors or audit firms.

10.3 We note that the CC is not minded to pursue the introduction of joint or component audit further, principally because (a) across the market the costs of its introduction could potentially be significant (although the CC has been unable to quantify what the level of costs might be), (b) investors were almost universally opposed to its introduction and (c) the introduction was considered to pose a potential risk to audit quality. The CC also considers that more frequent tendering and enhanced frequency of AQR team reporting (remedies 1 and 2) more effectively realise the advantage of giving companies greater visibility of firms' capabilities.

10.4 In drawing these conclusions, it appears that the CC has inappropriately grouped joint and consortia audit arrangements together, and thus assumed that the potential downsides of joint audit apply equally to consortia (or major component) audit arrangements. That is, arguments which have been put forward to counter joint audit have been used to dismiss the use of consortia audit arrangements.

10.5 First, contrary to the CC's assessment, consortia audits would not increase costs for the company and, in some cases, will result in a reduced audit fee for the entire group (as opposed to joint audit which is likely to lead to some increase in costs due to an inevitable duplication of audit effort/review by the two group auditors). Currently, almost all group audit arrangements operate with more than one audit firm involved in the audit of the various major components of the group, such as the case where overseas components are audited by a foreign affiliate of the group auditor. Incentivising or mandating a consortia audit arrangement where some of the components would have to be audited by affiliates from at least two different accounting networks, would therefore simply replace one subsidiary auditor with another, adding no additional costs or risk to an audit arrangement (assuming the subsidiary audit was undertaken by a firm of similar quality). The argument that consortia audits are likely to result in higher costs to a group should therefore be dismissed.

[7] A consortia audit is one where more than one auditor is involved in auditing the components of the group. The other audit firm would be responsible for auditing a significant part of the group (say at least 25%). A consortia audit allows participation of a non-dominant audit network in the audit of a large listed group but facilitates a dominant network alone signing the group audit report.

10.6 Further, there is no reliable academic evidence that indicates the adoption of consortia audits in other jurisdictions has resulted in a fall in audit quality. We are aware that some opponents of joint audit consider that it poses a risk to audit quality by creating the ability for something to "fall between the cracks", i.e. not be fully audited by either group auditor because both rely on the work of the other, but joint audit addresses that issue because each auditor takes responsibility for the whole group audit. This concern cannot be levelled at consortia audit, particularly as almost all large group audits already employ more than one auditor for the group audit arrangement (but where the other auditors in the group currently tend to be from the same accounting network), because each component auditor has defined responsibilities, and the group auditor has sole responsibility for the whole group audit opinion

10.7 Grant Thornton currently participates in a number of consortia audits of large international groups. Our experience is that the groups concerned are very satisfied in terms of both cost and quality (we have previously provided information to the CC on this area, in particular in our response to the CC's Issues Statement). Our experience is that, whilst many UK investors are opposed to the mandatory introduction of joint audit, there are many companies that are interested in employing a wider range of audit firms via a consortia audit arrangement. The argument that investors are almost universally opposed to consortia audit arrangements is therefore, in our view, not true.

10.8 Regarding the efficacy of introducing a consortia audit requirement, whilst we acknowledge the CC's view that mandatory tendering and enhanced AQR reviews and reporting will help to give companies a greater level of visibility of the capabilities of different audit firms, we consider that a consortia audit arrangement grants a company even greater (and more direct) visibility. This is because it allows a company to "test" a firm by using them (initially) for some smaller and (potentially) lower risk assignments on which it can then base its own assessment of their performance, not only with regards to audit quality, but also service quality. Since the cost of implementing consortia audit arrangements is close to zero, in our view this remedy provides a very effective way to achieve a reduction of barriers to entry and an expansion to the market for firms outside of the dominant players.

10.9 For the reasons set out above, we consider that consortia audit arrangements continue to be one of the most effective ways of increasing the visibility of companies to the capabilities of a wider range of audit firms. Where implemented, consortia audit arrangements should be transparent to a company's shareholders.

11. *Costs and benefits of the package*

11.1 The CC sets out in paragraph 5.91 of its provisional decision on remedies that a very small (0.0018%) change in the market capitalization of the FTSE 350 would mean that the benefit of the introduction of the package of remedies would exceed the costs.

11.2 In our view, there will be inevitable improvements in audit quality and corporate governance arising from the creation of a more competitive audit market for FTSE 350 companies and these benefits should not be underestimated. A likely outcome

of these same improvements in audit quality and corporate governance is that FTSE 350 companies will benefit from lower costs of capital, thereby creating significant value for investors[8]. There may also be spill-over benefits to investor confidence more generally, and therefore to listed companies from outside of the FTSE 350.

11.3 Furthermore, the costs of implementation of the package of remedies proposed by the CC are not disproportionate because the value (tangible and intangible) of a well-functioning audit market which will be created by its introduction, such as greater investor confidence in the capital markets, will be highly significant.

12. ***Implementation timetable and transitional provisions***

12.1 Overall, we support the CC's proposed timetable for the implementation of the package of remedies, which we consider is reasonable and will not impose unnecessary disruption upon the audit market or its main participants.

12.2 As noted earlier, one of the key requirements for mandatory tendering (and/or rotation) to be effective is sufficient and timely transparency of the timetable by which companies' will be undertaking these events. Transparency over these events is critical if companies and firms are to be able to properly plan and prepare for tender events, including for companies to assess which firms to invite to tender and for firms to assess which tenders to enter given their pre-existing knowledge and relationships with a company. The need for transparency will be particularly pertinent during the transitional phase when the date by which a company must tender will be based upon their last formal tender event and the date at which the current AEP is required to rotate - dates which will be unknown to many firms. We therefore propose that the CC introduces a requirement that companies must disclose in their Annual Report the date since the last tender and the date that the AEP is due to rotate.

[8] As stated by the European Commission: "Robust audit is key to re-establishing trust and market confidence; it contributes to investor protection and reduces the cost of capital for companies."
http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2010:0561:FIN:EN:PDF