



Johnson Matthey

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13 August 2013

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

Dear Sir/Madam

Statutory Audit Services Market Investigation

I am writing to you on behalf of the Johnson Matthey Plc Audit Committee which has discussed your provisional decision on remedies in relation to the audit market.

Whilst we agree with many of your proposed remedies we have a major reservation with regard to your proposal that FTSE 350 companies should put their statutory audit engagement out to tender at least every five years.

We believe that the recent changes to the UK Corporate Governance Code (the "Code") which require FTSE 350 companies to put their audit out to tender at least every ten years, or otherwise explain why they have not done so, have already had a major impact on the Audit Committee agenda. We believe that the Code's "comply or explain" principle lies at the heart of good governance in the UK and is well supported by companies and shareholders. This principle should rightly extend to audit tendering. As a result of the Code changes, we at Johnson Matthey have committed to tender the audit at some point in the next five years. Below is what we have said with regard to this issue in our 2013 Annual Report:

"In light of the changes introduced in the 2012 Code, which requires the external audit contract to be put out to tender at least every ten years (and which apply to Johnson Matthey for its year commencing 1st April 2013), and the FRC's transitional guidance, the Committee spent some time considering the merits of putting the audit out to tender in 2013/14. The Committee decided against this for a number of reasons including the fact that it is very comfortable with the performance of KPMG and is looking forward to working with the newly appointed lead audit partner, who will bring new perspectives to the audit. In addition there is the possibility of further changes in the relevant governance frameworks pending the conclusion of the Competition Commission's market investigation into the supply of statutory audit services to large companies in the UK, and best practice around the tendering process is also developing. Whilst the Committee does not propose that a tendering process should be undertaken

in 2013/14 it is committed to tendering the audit sometime during the new lead audit partner's five year tenure, at a time which is right for Johnson Matthey."

We believe this demonstrates that the Code is driving change, but importantly it is change which takes account of the needs of the business. We note that many other FTSE 350 firms have also made commitments to tender or have indeed announced firm plans to tender, and so for us it is clear that change is already happening in the audit market.

We note that one of your proposed remedies is to strengthen the accountability of the external auditor to the Audit Committee, including a stipulation that **only** the Audit Committee is permitted, inter alia, to negotiate and agree audit fees and the scope of the audit work. It appears that on the one hand the responsibility of the Audit Committee is being increased but on the other the Audit Committee is being disempowered of a key decision currently within its remit – that of determining the timing of putting the external audit out to tender. We feel that this is inconsistent and that Audit Committees should not be disempowered by putting an "order" on them.

We believe that having to tender the audit as frequently as every five years is likely to be overly disruptive to the business both during the tendering process itself and, if a change to external auditor is made following the tendering process, for a period of time thereafter whilst the new auditor learns the business. We believe that it is preferable to allow Audit Committees to enter this process at a time that suits the business and when they believe that it will enhance quality of the audit without causing the risk of undue business disruption. Otherwise there is a risk that tendering becomes merely a "tick box" process which is pointless, value destroying and does nothing to promote competition.

We further believe that such frequent tendering of the audit is likely to have a detrimental effect on audit quality, an absolutely fundamental issue for all Audit Committees. The auditors may well be distracted by having to spend additional time and resource on multiple tendering processes whilst companies may feel under undue pressure to change their auditors regularly thereby impacting audit quality in the short-term: just as quality is improving, companies will need to start thinking about tendering again.

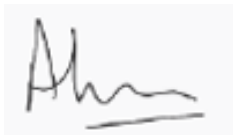
The cost of a proper audit tender is significant both financially in terms of the costs to the audit firms tendering, but also in terms of management time within the business. Therefore a tender should only be entered into when the Audit Committee feels that the business is likely to gain from such a process, not just to comply with an enforced "order" or "rules-based" system which runs counter to the comply or explain principle of the Code. If FTSE 350 businesses are forced to tender their audit every five years, costs will rise but quality may decline, this cannot be an outcome that any stakeholders would welcome.

Under the current Code regime, should a company choose not to comply with the Code provision on timing of audit tendering, shareholders have every right to challenge a company's explanation. Ultimately shareholders have the ability to vote against the re-appointment of the auditor as well of course the directors, including the Audit Committee chair, if they feel that is appropriate. Even if companies do comply with this provision, shareholders can still exercise these rights if they have concerns over the quality and effectiveness of the external audit. Therefore there are already mechanisms in place to allow the shareholders influence in this area and this is being further

strengthened by the increased disclosure requirements being imposed on Audit Committees, which we support.

In summary, we fully support the changes made to the Code in relation to audit tendering and believe that these are already having a positive impact but we are against the “order” which will force us to tender the audit every five years. We see no merit in being forced into tenders. We have accepted the principle of more regular tendering on a comply or explain basis, such tendering to take place at a time that works for the business, and our shareholders have greater exposure to our thinking in this regard and mechanisms to act if they disagree.

Yours faithfully

A handwritten signature in black ink, appearing to read 'Alan', with a horizontal line underneath the name.

Alan Ferguson
Chairman - Audit Committee