

THE STATUTORY AUDIT SERVICES FOR LARGE COMPANIES MARKET INVESTIGATION

The Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014

Notice of intention to make an Order under section 165 of and Schedule 10 to the Enterprise Act 2002 and public consultation on the proposed Order

Background

1. On 21 October 2011, the Office of Fair Trading (OFT), in exercise of its powers under sections 131 and 133 of the Enterprise Act 2002 (the Act), referred the supply of statutory audit services to large companies in the UK to the Competition Commission (CC) for investigation and report.
2. The CC investigated the matters referred to it pursuant to sections 131 and 133 of the Act and, in accordance with section 134(1) of the Act, concluded that there are features of the market or markets which, either alone or in combination, prevent, restrict or distort competition in connection with the supply of statutory audit services to large companies in the UK and, in accordance with section 134(2) of the Act, that there were adverse effects on competition (AECs). The CC published its findings in a report under section 136 of the Act entitled *Statutory audit services for large companies market investigation: a report on the provision of statutory audit services to large companies in the UK* and notified on 15 October 2013 (the Report).
3. The CC considered, in accordance with section 134(4) of the Act, whether (a) action should be taken by it for the purpose of remedying, mitigating or preventing the AECs or any detrimental effect on customers; and whether (b) it should recommend the taking of action by others for the purpose of remedying, mitigating or preventing the AECs or any detrimental effect on customers; and (c) in either case, if action should be taken, what action should be taken and what is to be remedied, mitigated or prevented.
4. In the Report, the CC decided on a package of remedies to address the AECs that it found. The remedies included:
 - (a) that companies listed on the FTSE 100 and FTSE 250 indices must put their statutory audit services engagement out to tender not less frequently

than every ten years. The CC was of the view that many companies would benefit from going out to tender every five years but if they choose not to, then the Audit Committee should set out in the Audit Committee Report the financial year in which it next plans to go out to tender and why going out to tender in this year is in the best interests of its members;

(b) measures to strengthen the accountability of the auditor to the Audit Committee, including a stipulation that only the Audit Committee is permitted to negotiate and agree audit fees and the scope of audit work, influence the appointment of an audit engagement partner, initiate and supervise competitive tender processes, make recommendations for appointment of auditors and authorise the auditors to carry out non-audit services; and

(c) that provisions in loan agreements which restrict a company's choice of auditor to lists or categories should be prohibited, although parties may require that any auditor should meet objectively justified criteria.

5. On 1 April 2014, the functions of the CC transferred to the Competition and Markets Authority (CMA) pursuant to Part 3 of the Enterprise and Regulatory Reform Act 2013 and the Enterprise and Regulatory Reform Act 2013 (Commencement No 6, Transitional Provisions and Savings) Order 2014.
6. By virtue of section 138(3) of the Act, the remedies implemented by the CMA must be consistent with the findings in the Report unless there has been a 'material change of circumstances' or other 'special reason' for deciding differently since preparation of the Report.
7. Since publication of the Report, the European Parliament and the Council have adopted measures reforming the statutory audit market, namely Directive 2014/56/EU (the Directive) and Regulation (EU) No 537/2014 (the Regulation). The CMA considers that this constitutes such a material change of circumstance or special reason to justify taking these measures into account in implementing the remedies decided upon in the Report.
8. In particular, under the Regulation, public interest entities (PIEs) are required to change their statutory auditor every ten years. Member states can, however, by way of derogation, permit shorter rotation periods, and by way of further derogation, allow PIEs to extend the audit engagement to up to 20 years provided that retendering takes place at least every ten years.
9. The CMA has considered the provisions of the Regulation and in particular the transitional provisions in Article 41.

10. The CMA now gives notice of its intention to make the proposed Order on mandatory use of competitive tender processes and Audit Committee responsibilities.
11. The CMA further notes that measures adopted in both the Directive and the Regulation prohibit contractual clauses restricting the choice of statutory auditor to certain categories or lists in all third party contracts. The CMA welcomes these measures and considers that these measures are more extensive than its proposed remedy on auditor clauses in loan agreements, and therefore sufficiently address concerns identified in its Report in this regard. In light of this 'material change of circumstances' or 'special reason', the CMA is not minded to pursue its remedy on auditor provisions in loan agreements.
12. The CMA invites written representations on the proposed Order from any interested person or persons.
13. This notice and the draft Order, together with an Explanatory Note, have been published on the CMA website.
14. The CMA will have regard to any representations made in response to this Notice. The CMA may also make modifications to the proposed Order as a result of any representations. If the CMA considers that any representation necessitates any material change to the proposed Order, the CMA will give notice of the proposed modifications.
15. Representations should reach the CMA by 5pm on 24 August 2014. Representations should be in writing and should be addressed to:

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Southampton Row
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or by email to: denis.kelly@cma.gsi.gov.uk

(signed) Laura Carstensen
Group Chair
24 July 2014