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Statutory audit market study
Competition and Markets Authority
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Johnson Matthey response to the statutory audit market study update paper

Dear Sir/Madam

Johnson Matthey welcomes the opportunity to comment on the proposals in the CMA update paper on the statutory audit services market study and are in favour of any outcomes which improve audit quality. Given the short timelines for a response we have commented on what we regard as the main themes in the proposal, those being regulatory scrutiny, mandatory joint audits, market share caps, the division of audit and non-audit services and peer reviews.

Regulatory Scrutiny

As stated in our previous response we believe in shareholders using the powers they already have to respond to audit committee decisions that they do not support and we would welcome shareholders being more active in this regard. The Regulator already has the ability to meet with the Audit Committee. We encourage them to use this power and are supportive of engagement, however the current recommendation risks being overly bureaucratic.

To extend the scope of their role as suggested, the regulator would have to recruit a team who have the expertise and independence to undertake this role and agree terms of reference that would have to deal with, amongst other things, what happens in a dispute as there is the potential for the regulators views to be at odds with the wishes of the Board and possibly the shareholders.

Joint Audits

As we stated previously we don't support the imposition of joint audits. There is little empirical evidence from anywhere in the world that audit quality is enhanced and we note that the Competition Commission in 2013 said that "Whilst we accept that joint/shared audit has some benefits in relation to lowering barriers to entry, expansion and selection, we were not convinced these benefits were significant, or certain, and did not justify the potential costs of such a remedy".

Audit quality is paramount and our concern is that there is greater potential for audit quality to suffer than be enhanced by this proposed remedy. The complexity of it is ably demonstrated by paragraphs 4.30 – 4.39 in your paper which details the need for regulatory oversight as there will be issues around the way the auditors are to be selected and allocated work. This complexity could easily lead to unintended consequences.

We remain more supportive of shared audits as whilst this would bring a substantial change to the market it is a lower risk option and one which is worthy of more consideration.

Market Share caps

A market share cap, however structured, will have unintended consequences, many of which are a threat to audit quality; it could disempower shareholders and audit committees, a cap, by its nature, is anti-competitive and the mechanism by which it might be implemented could impede an Audit Committee selecting the firm best placed to improve audit quality.

Division of audit & non-audit services

We share a concern around issues such as profit pooling resulting in audit partners benefitting from non-audit profitability and are in favour measures to encourage the transfer of knowledge, audit technology, people and skills between the "big four" and the challenger firms.

However, it is hard for us to judge what the issues are with an operational split at the multi-disciplinary firms and we worry what impact this really will have on international companies like ours given that audit related services around the world will be provided by non UK audit only firms.

We are clear that if an operational split is introduced that it be introduced for the "big four" and the challenger firms. We cannot have a situation where a challenger firm is both the auditor and provider of non-audit services without having the appropriate independence safeguards in place. If those safeguards are right for a "big four" firm they must also be right for a challenger firm.

Peer Reviews

As you conclude in paragraph 4.155 you do not consider peer review an effective way to improve choice and resilience. This is therefore about driving audit quality. We would much rather this remedy be linked in with the proposed enhancement of the AQR process run by the FRC.

Carrying out a peer review during the audit would place additional pressure on the auditor and may well have the unintended consequence of decreasing audit quality if the auditor and the company divert time and resource to manage the peer review. In the case of mandatory joint audits a further peer review would be somewhat duplicative.

Finally given the number of studies being carried out on the audit market we would hope that before any final commitments are made that a review is carried out to ensure the totality of the recommendations fit together in a cohesive way and that there are no duplicate or conflicting proposals.

We hope you find our comments helpful.

Yours faithfully,

Alan Ferguson
Chair of Audit Committee

Anna Manz
Chief Financial Officer